S. HRG. 100-941

SOFT DRINK MANUFACTURERS PRACTICES

HEARING

BEFORE THE

SUBCOMMITTEE ON THE CONSUMER

OF THE

COMMITTEE ON COMMERCE, SCIENCE, AND TRANSPORTATION UNITED STATES SENATE

ONE HUNDREDTH CONGRESS

SECOND SESSION

ON

S. 2347

TO DECLARE CERTAIN ACTIVITIES OF MANUFACTURERS OF SOFT DRINKS TO BE UNFAIR ACTS OR PRACTICES FOR PURPOSES OF THE FEDERAL TRADE COMMISSION ACT

SEPTEMBER 28, 1988

Printed for the use of the
Committee on Commerce, Science, and Transportation

U.S. GOVERNMENT PRINTING OFFICE

91-933 O WASHINGTON : 1988

5261-17

For sale by the Superintendent of Documents, Congressional Sales Office
U.S. Government Printing Office, Washington, DC 20402

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SOFT DRINK MANUFACTURER'S PRACTICES

WEDNESDAY, SEPTEMBER 28, 1988

U.S. SENATE,
SUBCOMMITTEE ON THE CONSUMER,
COMMITTEE ON COMMERCE, SCIENCE, AND TRANSPORTATION,
Washington, DC.

The subcommittee met, pursuant to notice, at 2 p.m., in room SD-222, Russell Senate Office Building, Hon. Daniel K. Inouye presiding.

Staff members assigned to this hearing: Kevin Curtin and Linda Lance, staff counsels; and Chuck Harwood, minority staff counsel.

OPENING STATEMENT BY SENATOR INOUYE

Senator INOUYE. The bill before this Committee this afternoon, S. 2347, declares certain activities of soft drink manufacturers to be unfair for the purposes of Section 5 under the FTC Act.

This bill specifically refers to certain acts of any person engaged in the business of manufacturing, selling or distributing post-mix soft drink dispensing equipment or engaged in the business of manufacturing, selling, bottling or otherwise distributing soft drink syrup to be declared unlawful.

The witnesses that we will hear from today represent independent companies scattered across the United States. They supply the equipment and syrup necessary to dispense soft drinks at bars, restaurants and fast food outlets. Over the years these distributors have served the outlets that large manufacturers did not service.

However, in their efforts to further monopolize the soft drink market, the Committee has been advised that large soft drink manufacturers have started to provide at little or no cost beverage-dispensing equipment to potentially large retail customers in order to lure them away from their competition.

This we believe creates an unspoken obligation to purchase the soft drink syrup from the company giving away the equipment.

Furthermore, when these large syrup manufacturers install the beverage-dispensing equipment at no charge the equipment usually has just sufficient dispensing outlets on the unit to handle the syrup flavors that the manufacturer produces, leaving no room for the restaurant or tavern owner to dispense soft drinks of a competitor.

The impact on the beverage-dispensing equipment industry is twofold. First and most dramatically, I believe that it will undermine the survival of those companies, as I believe we will hear today, whose very existence is dependent upon the sale or lease of beverage-dispensing equipment.

Second, once the equipment is installed, I believe that the customer invariably purchases syrup directly from the large manufacturer. Thus the equipment industry is not the only victim of this anti-competitive practice.

We believe that consumers and other distributors may suffer as well. Therefore, it is the Committee's hope that this hearing will be the beginning of a closer look into this matter.

With both this Committee and the Senate Judiciary Committee studying this matter, I believe that a fair assessment of this situation can be made. In all candor, it is my hope that it will not be necessary to enact any legislation, but that out of this inquiry the soft drink industry will work with both committees to find a viable solution to the problem.

[The bill follows:]

100TH CONGRESS
2D SESSION

S. 2347

To declare certain activities of manufacturers of soft drinks to be unfair acts or practices for purposes of the Federal Trade Commission Act.

IN THE SENATE OF THE UNITED STATES

APRIL 28, 1988

Mr. INOUYE introduced the following bill; which was read twice and referred jointly to the Committees on Commerce, Science, and Transportation and the Judiciary

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A BILL

To declare certain activities of manufacturers of soft drinks to be unfair acts or practices for purposes of the Federal Trade Commission Act.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That (a) it is an unfair act or practice, for purposes of section 5 of the Federal Trade Commission Act (15 U.S.C. 45), for any person engaged in the business of manufacturing, selling, or distributing postmixed soft drink dispensing equipment or engaged in the business of manufacturing, selling, bottling, or otherwise distributing soft drink syrup, to induce (directly or indirectly or through an affiliate), using any of the means

described in subsection (b), any retailer engaged in the sale of postmixed soft drinks to purchase any soft drink syrup from such person to the exclusion in whole or in part of soft drink syrup sold or offered for sale by other persons in interstate or foreign commerce, if—

(1) such inducement is made in the course of interstate or foreign commerce;

(2) such person engages in the practice of using any such means to such an extent as substantially to restrain or prevent transactions in any soft drink syrup in interstate or foreign commerce;

(3) a direct effect of such inducement is to prevent, deter, hinder, or restrict other persons from selling or offering for sale any soft drink syrup to such retailer in interstate or foreign commerce; or

(4) a direct effect of such inducement is to prevent, deter, hinder, or restrict other persons from furnishing, leasing, selling, or servicing any postmixed soft drink dispensing equipment or postmixed soft drink dispensing equipment systems to such retailer in interstate or foreign commerce.

(b) The means of inducement referred to in subsection (a), with respect to a retailer, are—

(1) furnishing without consideration, giving, or lending any postmixed soft drink dispensing equipment,

postmixed soft drink dispensing equipment systems, fixtures, signs, supplies, money, services, or other things of more than nominal value to the retailer;

(2) leasing or selling at below fair market value, any postmixed soft drink dispensing equipment, postmixed soft drink dispensing equipment systems, fixtures, signs, supplies, money, credit, services, or other things of more than nominal value to the retailer; or

(3) extending credit to the retailer for a period in excess of the credit period that is usual and customary in the soft drink distribution industry for the particular class of transactions.

(c) As used in this Act, the term "postmixed soft drink dispensing equipment" means all of the components used to produce carbonated water and to mix soft drink syrup with carbonated water as the soft drink is dispensed from a faucet.

(d) Subsections (a), (b), and (c) shall take effect on the date which is 60 days after the date of enactment of this Act.

Senator INOUYE. We have many witnesses this afternoon, and we have divided these witnesses into three panels. Our first panel will consist of the President of Jason Soda Systems, Inc., of Connecticut, Mr. Brook R. Jason, and the President of Damon Distributors of Nevada, Mr. Douglas S. Damon, and a representative of the National Licensed Beverage Association of Washington, Ms. Loretta Lippy.

Mr. Jason, Mr. Damon, and Ms. Lippy.

STATEMENT OF BROOK R. JASON, PRESIDENT, JASON SODA SYSTEMS, INC.

Mr. JASON. Good afternoon, Senator Inouye. My name is Brook Jason. I am often called Bud Jason. I am the President of Jason Soda Systems, Inc., of South Windsor, Connecticut, which is a suburb of Hartford.

First I would like to personally thank you for sponsoring S. 2347. It is truly an honor to appear before you, one of America's most decorated heroes and respected Senators.

Sitting with me is counsel for CEEGA, the Committee to Eliminate Equipment Give-Aways, Stanley Bregman, of the firm Bregman, Abell & Kay here in Washington.

In addition, I would like to tell you that I am a charter member of the NBDEA, the National Beverage Dispensing Equipment Association, which was formed in 1969. And I am also a member of the NSDA, the National Soft Drink Association.

Al Griggs is here today, who is Vice Chairman of the National Soft Drink Association, representing the opposition. And I must tell you that he certainly does not represent my views, as well as a number of other independents in the soft drink industry.

In 1945, my father, Isy Jason, whose parents owned a soda fountain in Bristol, Connecticut, had a problem finding a company to repair that soda fountain. From that need he created a company to install and service soda fountain equipment in the Connecticut area.

Some of you recall that soda fountains were common in drugstores in the 1930s and 1940s. Our industry's roots go back to the sale, installation and repair of soda-dispensing equipment.

In the early days of our business, carbonated water was dispensed from a draft arm and mixed with syrup from a syrup pump in the soda fountain rail. Many people here can recall having vanilla or cherry coke by having the syrup and carbonated water stirred together. The development and use of this equipment gave birth to our industry.

As technology progressed, equipment was developed to dispense a mixture of carbonated water and fountain syrups automatically. Hence the name fountain-dispensing business used by several of the national syrup manufacturers.

The mixing of carbonated water and syrup at the point of dispensing is called post-mix. This is interesting to note the distinction, because this differs dramatically from pre-mix, which is nothing more than bottled or canned soda sold in bulk, ordinarily five-gallon containers.

Soft drink bottlers traditionally derived their greatest revenues from the profits from cans, bottles and pre-mix. To many bottlers, post-mix merely was sampling to drive can and bottle sales.

We developed our business from providing carbonation systems and fountain syrups to restaurants, taverns, soda fountains and a variety of other food service concerns. Our revenues in the early years came from the renting of this type of equipment, along with the supply of carbonic gas used to make the carbonated water.

In our case we also supplied the fountain syrups that were used in conjunction with the carbonation system. I am proud to say that we have been a Coca-Cola fountain syrup wholesaler for over 40 years.

Coca-Cola, unlike Pepsi-Cola, has used independent wholesalers as well as bottlers to distribute their product. Today we are the largest Coca-Cola fountain syrup wholesaler in the State of Connecticut, and the second largest in New England. In addition, we also sell brand 7 Up, Sunkist, Canada Dry and a line of products that we make under our own label.

My father, Isy Jason, established this business by renting equipment to restaurants who needed service to this type of equipment around the clock. Service was a key issue. We serviced our customers seven days a week, 365 days a year.

In today's difficult labor market in New England, many of you realize I am sure that this is no easy task. We are faced on a continual basis with rising costs of insurance, both liability insurance and health insurance, as well as ever-increasing labor rates, vehicle costs, gasoline and many other overhead expenses.

In our market specifically, McDonald's pays part-time help $8 an hour to make hamburgers and serve fries. We work from there up.

Having started the business from scratch with essentially no capital, the revenue was generated out of a reasonable rate of return on the rental of the equipment. And we built capital and in turn expanded the business from that basis.

For over 40 years we have purchased and rented equipment to smaller outlets throughout our marketplace. Our markup was based on an 18-month rate of return on our equipment and installation costs, which frankly is not uncommon in the rental of any type of equipment, not just soft drink or restaurant food service equipment.

I am saddened to tell you that in recent years it has become difficult to rent equipment and sell fountain syrup at a reasonable markup because of policies and forces in the marketplace directly attributable to the two dominant cola manufacturers in the industry.

Namely, what we see is equipment being loaned or leased at low cost to smaller outlets, and syrup being sold to these same outlets, sometimes at wholesale cost or even below our cost.

In the early years of our business Coca-Cola USA, a division of the Coca-Cola Company, and Pepsi-Cola, while interested in the national restaurant chains, frankly were not active in the individual owner-operator accounts.

The marketing programs offered by Coke and Pepsi have always been available to large national accounts. Such programs often include the placement of dispensing equipment on loan, marketing

assistance, as well as payment of marketing funds merely for the sale of their products.

In the late 1940s when we began in the syrup distribution business, Coke and Pepsi had their flagship brands only, and no other allied products were manufactured.

In recent years, however, Coke and Pepsi have developed and marketed a full line of products to meet the customers' taste for the lemon and lime segment and other fruit flavors and diet beverages. With these added products, they now wanted total control of the account.

As Coke and Pepsi's business grew in the national account market over the years, the business of our industry members grew in the smaller volume account.

Our business grew dramatically over the years until about five years ago. We projected planned growth from the placement of new accounts, additional rental income, more sale of carbonic gas and syrup. Now market pressures from the cola manufacturers are such that we cannot compete.

Traditionally we have gone to equipment manufacturers and purchased countertop refrigerated dispensing equipment and other post-mix equipment at the most competitive prices we could secure, and approached our customer base to lease, rent or purchase this equipment from us. Our rates have historically, again, been established on the basis of returning our money in 18 months.

Now we find ourselves in the same marketplace, with the syrup manufacturers often times purchasing equipment in largè buying power at significantly lower costs, without the same rate of returns being necessary. In many cases, they do not rent, lease or sell the equipment.

Recently, we experienced a situation where our Pepsi-Cola bottling company in the Hartford, Connecticut area was purchased by an out-of-state conglomerate. They wanted to stake their claim in the post-mix business in our marketplace because they were previously not involved.

They virtually went up and down the street to every fountain account and offered free or leased equipment at ridiculously low rates, sometimes as little as $1 a week, to get the account.

We had two mechanics two years ago who almost daily had a route of going around, picking up equipment that the Pepsi-Cola bottler had removed from our accounts and put in the back room.

You might ask, how can they do this and for how long? Well, when that bottling company was purchased it was common knowledge that over a half a million dollars of equipment was shipped into their warehouse for placement on the street, the charge to the sales department being, "Get it out there; do whatever you have to do to get it out there."

How can it be done? We know for a fact that, and it has been freely admitted that the national manufacturers, specifically in this case Pepsi-Cola, provided large amounts of money under the guise of marketing funds, or advertising allowances, to subsidize that equipment placement program.

In addition, Mr. Griggs, who is here in the room, is president of the Coca-Cola bottling company of Northhampton, Massachusetts, I believe is a marketing wholesaler for the Coca-Cola Company.

The marketing wholesaler program for Coca-Cola, as I understand it, essentially funds a bottler in a given market area for distribution of product with the dollars being available to spend on whatever he sees fit to spend them on. These programs, quite frankly, are not available to us.

One of the most blatant situations that we see in our marketplace is a different deal being offered to each and every restaurant up and down the block. Two years ago when we saw the Pepsi-Cola bottler get aggressive, we determined that their strategy was to have no strategy at all.

We could not go out and talk to our customers about what the bottling company was proposing, because it was a different arrangement everywhere they went, and they could call on two accounts next door to one another who did the same volume but were offered two different programs.

Frankly, we are caught in the proverbial squeeze play. I honestly do not believe that either Coke or Pepsi would like to have our firms out of business.

But in an effort from a competitive standpoint to get more market share, we find ourselves in a position where we do not have the staying power, at least many of the individuals in this room, to meet long-term this type of unfair competition.

It is interesting to note that our rental prices on equipment today, in an attempt to compete with Pepsi in our market, are significantly lower, *lower,* than they were three years ago.

As both Coke and Pepsi have expanded their free or loan programs to any and all accounts, we see no future expansion of our business. In fact, just survival may be very difficult.

Unlike some of my contemporaries in the industry, we have been financially sound enough up to this point to stay in business. Realistically, however, we do not think we can continue much longer.

These practices must stop if we are to survive. Survival frankly for some of us has not been possible, and some of my peers sitting in this room have all but been starved out of their businesses. Some were lucky enough to cash out part of their investment by selling to a local Coke or Pepsi bottler.

Several years ago I was approached by a senior vice president of one of the major syrup manufacturers with regard to selling my business. I told him it was a business I enjoyed, I was second generation, and as with many family businesses hope my children who are in this room will have the opportunity, if they have the desire, to follow me in this business.

This executive suggested that my ideals were not realistic, that in fact we in our business in the long run would probably not exist because the cola manufacturers are acquiring more and more independent bottling companies, and will eventually acquire businesses like ours one way or another. He said I should be content to get a fair price and sell out to a bottling company and pursue other interests.

Quite obviously, I was not intimidated by the picture he painted, and told him I would continue to make my mark in this industry for some time to come. As the Cola wars escalate, I must say I sometimes question my ideals as to whether they are realistic.

We cannot compete with free equipment. We cannot compete with small margins on syrup and still cover our overhead. But the question I ask you here today is why should we have to compete with these grossly unfair trade practices when everything they stand for is unjust?

I often wonder if the sales personnel of either of the major cola giants had to go out and truly sell their product, relying on their own sales skills and the quality of their product, how many accounts they would have today.

Both of these companies have grown in the fountain syrup business with the help of, and at the expense of, companies like ours who have represented them well over the years.

Now that we have helped to develop their business in a significant way, must we fall by the wayside? There is certainly something wrong with American business philosophy if two dominating giants can destroy our industry in the desire to become number one. Thank you.

Senator INOUYE. Thank you very much, Mr. Jason. In your testimony you have indicated that you have been a major dispenser of Coca-Cola syrup since the 1940s.

Mr. JASON. That is correct.

Senator INOUYE. In fact if I recall you testified that you are the second largest in the nation?

Mr. JASON. In New England.

Senator INOUYE. In New England. That being the case, did you not benefit from the activities of Coca-Cola in your area?

Mr. JASON. In our case, as the Coca-Cola wholesaler, we were buying and renting equipment directly to customers. And dispensing brand Coca-Cola through the dispensing equipment at our normal margins on equipment rental, as well as on syrup sales. So as a wholesaler we had an opportunity to generate profit dollars from a fair markup.

We are also, however, wholesalers of brand 7 Up and Sunkist and other flavors as well, that we also see profit margins on.

Senator INOUYE. But Coca-Cola was not competing with you in selling syrup?

Mr. JASON. No. I must say that in our marketplace, as a loyal Coca-Cola wholesaler, we did not compete directly with the fountain department of Coca-Cola.

As a matter of fact, some of the individuals in this room know us to be Coca-Cola, in the State of Connecticut specifically, because the bottler in our marketplace has not seen fit to get involved in post-mix dispensing, and we work very well with our Coca-Cola bottler.

Senator INOUYE. Did this practice have any effect on the consumer? We are talking about you now and Coca-Cola. What about the person who buys it? Has the price gone up or down?

Mr. JASON. What we see most often is from a pricing standpoint, that while syrup prices and equipment prices may have come down the restauranteur who dispenses the product in fact has not adjusted his prices accordingly to the consumer.

The other thing I think that we see most often is that when equipment is placed that is owned by the parent company, or a bottling company, of either Coca-Cola or Pepsi-Cola, that the choice of

products is not available to the consumer that might ordinarily be available.

Quite frankly, how many restaurants can we walk into today and ask for either a Coke or a Pepsi and have the opportunity to get either one? Usually it is one or the other. And if you get a Coke, in all probability you will get Sprite and Diet Coke and Fanta Root Beer and Fanta Orange, which are also products of the Coca-Cola Company.

Senator INOUYE. Since the larger companies began this practice, do you have any statistics to indicate how many have gone down under?

Mr. JASON. How many companies in our industry——

Senator INOUYE. Have failed, yes.

Mr. JASON. Personally, I know of at least 10 companies who are no longer in the soft drink dispensing equipment business.

Some of them have diversified into other product lines. There are a number of others, but I know of personally only 10 who are involved in our trade association in the business.

There are approximately 300 to 400 independent companies in the country who do what we do.

Senator INOUYE. Thank you very much.

[The following information was subsequently received for the record:]

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United States Senate
COMMITTEE ON COMMERCE, SCIENCE,
AND TRANSPORTATION
WASHINGTON, DC 20510-6125

October 13, 1988

Mr. Brook R. Jason
Jason Soda Systems, Inc.
145 Edwin Road
South Windsor, CT 06074

Dear Mr. Jason:

Thank you for your participation in the Consumer Subcommittee's hearing on S. 2347, regarding certain trade practices in the soft drink industry. As you know, Committee members often have written follow-up questions for the witnesses at such hearings.

Since I was unable to attend the hearing, I would appreciate your response to several written questions which are enclosed with this letter. Your responses will be made a part of the hearing record along with your testimony. In order that the hearing record may be printed promptly, I would appreciate your response to these questions within two weeks, no later than October 26, 1988. Please address your responses to the Consumer Subcommittee of the Committee on Commerce, Science and Transportation, Room 227 Hart Senate Office Building, Washington, D.C. 20510. If you have any questions, please contact Linda Lance, Staff Counsel to the Subcommittee, at (202) 224-0415.

Thank you for your assistance to the Committee.

Sincerely,

ALBERT GORE, JR.
Chairman
Consumer Subcommittee

Enclosure

AG:llc

QUESTIONS OF SENATOR GORE FOR MR. JASON, JASON SODA SYSTEMS, INC.

1. I understand that your business includes the rental of fountain equipment as well as the sale of fountain syrup. Do your rental agreements with your customers require the purchase of any of your syrup? Do they relate in any way to the sale of syrup?

2. What is the normal term of your rental agreements with your customers for fountain equipment?

3. Can the rental agreements between you and your equipment customers be terminated at will by either party or is there a contractual agreement for a particular time period?

4. Based on your experience, when the syrup companies loan equipment for free or at a reduced price do they always require the recipient to buy a certain kind of syrup? When purchases of syrup are required, must the purchases be made directly from the syrup company, or can the recipient of the equipment buy syrup from an independent wholesaler?

5. Are you aware of any independent syrup wholesalers that loan equipment for free or at a reduced price?

6. If S. 2347 is passed, will that result in higher overall costs for fountain beverages to retailers, particularly restaurants and taverns? If so, are those increased costs likely to be passed on to the retailers' customers?

7. Do any of your customers who rent fountain equipment from you or own their own equipment offer both Coke and Pepsi, or more than one brand of any flavor of soda? If so, what percentage of your customers do that?

8. Do both Coke and Pepsi invest in research and development of fountain equipment? If so, in your judgment is that an element of competition between Coke and Pepsi? Could S. 2347 reduce that competition?

9. Have you tried to market your fountain equipment to Coke and Pepsi for their use in their free or reduced price equipment programs? If not, why not? If so, what was the result?

91-933 0 - 89 - 2

October 26, 1988

Senator Albert Gore, Jr.
Chairman
Consumer Subcommittee
United States Senate
Committee on Commerce, Science, & Transportation
Washington, D.C. 20510-6125

Dear Senator Gore:

Thank you for your letter of October 13, 1988, with respect to clarifying some of the issues with regard to Senate bill S.2347, and the following is my response to your specific questions.

1. Jason Soda Systems leases a variety of beverage dispensing equipment and other specialty food service equipment and has since 1945. Our rental agreements are predicated on a reasonable rate of return on our investment, which also includes the installation and maintenance of said equipment in various accounts. A copy of our agreement is attached for your perusal. You will note that there is no mention made of the purchase of products in this agreement, nor is there any implied or oral agreement to purchase syrup or other products. We do however, sell fountain syrup to a number of customers who rent soda dispensing equipment from us. Occasionally preferred pricing on syrup may be given to a customer who also rents his soft drink equipment from us.

2. Our normal term of a rental agreement is two years. However in some cases where we make a major capital investment in special equipment for a customer, the agreement may be 3, 4, or 5 years. On rare occasions, in the turnover within the restaurant trade, we will write a 1 year agreement if it covers an installation that had been made sometime ago but where new ownership is now involved.

3. Within the body of our agreement, you will find that the termination can be effected by the customer with a 30 day notice prior to the anniversary date of said agreement. We also have that same right.

Jason
Jason

CORPORATE HEADQUARTERS
145 Edwin Road, South Windsor, Connecticut 06074
(203) 289-7478 FAX (203) 528-1613

MEMBER N.B.D.E.A.

4. As a matter of course Coca-Cola USA or the Pepsi Cola Company loan equipment, it is common for only the Coke or Pepsi family of products to be dispensed on that loaned equipment. There has been a policy in recent years of allowing one valve on a soft drink dispensing system to be used for a non Cola product not of that Cola company's manufacture; however as a practical matter, rarely is this the case. In actuality, it is unlikely that any syrup supplier would deliver only one product to a particular restaurant when no other products or services are being purchased. It is simply not economical to do so. The source for the product where equipment is placed on loan and where the syrup manufacturers can in fact vary the product, can come through a national account billing arrangement directly from the syrup manufacturers headquarters. In the case of Coca-Cola, a "desk jobber" may be assigned to bill the product with a local delivery agent being paid to make the delivery. Additionally, an independent wholesaler such as a bottler or company like our own may be assigned to deliver product to that customer on behalf of Coca-Cola.

5. At this time, I am not aware of any independent syrup wholesalers loaning equipment for free. However, preferred pricing may be available should an independent syrup wholesaler enjoy all the product business in a specific account. My knowledge is essentially from the New England marketplace where these practices do not occur.

6. If S.2347 is passed, it is highly unlikely to result in higher overall costs for fountain beverages to retailers. We believe that the price of fountain syrup should in fact come down as the price of equipment will now be separate from the price of syrup. We believe the existing gallon of syrup sold in the industry already includes significant costs to cover the loan programs currently being implemented by Coca-Cola USA and Pepsi Cola. Therefore, we feel it is highly unlikely that the retailer or the ultimate consumer will be adversely impacted by this program.

7. Within our fountain marketplace and in our customer base, a very small percentage of customers dispense both Coke and Pepsi as fountain soda beverages. Specifically, in the Fairfield County area of Connecticut, adjacent to Pepsi Cola Headquarters in New York, there are several restaurants who buy their Cola-Cola fountain syrup from us, but also dispense Pepsi Cola because they are frequented by the corporate personnel of Pepsi Cola. With the exception of the colas, we do not find other like brands being dispensed within the same account.

8. We believe both Coca-Cola USA and Pepsi Cola invest heavily in the research and development of fountain dispensing equipment. However, it should also be noted that there are many equipment manufacturers eager for state of the art, who design and build equipment of a competitive nature available to the trade, regardless of the product being dispensed. We see both manufacturers touting the excellence of their research and development departments. However, we in the beverage dispensing equipment industry whose primary source of income comes from sale and lease of high quality equipment are probably the best source of research and development information with respect to product design and quality.

9. For many years we have tried to market our equipment to Coca-Cola USA however, it should be noted that the major equipment manufacturers have established relationships directly with the parent companies of both Coke and Pepsi to sell equipment at preferred pricing (in some cases lower than our cost) therefore, the viability of our selling equipment to either Coke or Pepsi within our marketplace is not realistic. As a matter of fact, the equipment manufacturers are advised that if they do not make their equipment available to the parent syrup company at a reduced cost they will not be favored with the equipment business. In an effort not to lose prospective equipment sales to Coke and Pepsi their demands are often met.

In closing, I believe it is important to note that our industry, specifically those of us whose primary business is the lease and sale of beverage equipment, is being severely harmed by the trade practices of Coke and Pepsi in the marketplace. As we understand it, their primary business should be the sale of their product-their fountain syrup. It is the inducements offered in the form of free equipment and services to effect exclusive placement of product that is preventing our businesses from being profitable and is slowly killing our industry.

Respectfully,

Brook R. Jason

Brook R. Jason
President

Senator INOUYE. Mr. Damon.

STATEMENT OF DOUGLAS S. DAMON, PRESIDENT, DAMON DISTRIBUTORS

Mr. DAMON. Thank you, Chairman Inouye. My name is Doug Damon. I own a company in Sparks, Nevada called Damon Distributing Company. I have been in the business that Mr. Jason described for a number of years. Effectively I am out of that business now, and that is what I am here to talk to you about today.

We have been in the business of selling, renting, and leasing soft drink dispensers and the syrups that goes along with the dispensers for a number of years, as I said. And we were effectively put out of the syrup business and the equipment business by the equipment give-away programs.

To describe my market a little bit, we are in a market that is small in the number of people, less than half a million. But we attract a great number of tourists. So from that standpoint, there are large volume accounts, specifically casinos and ski resorts.

For years I had competed effectively in those accounts, based upon my ability to manufacture my own syrup and to get equipment into the account on at least a cost basis. Those times have changed.

To capsulize, the Coca-Cola and Pepsi-Cola companies have found my Achilles' heel, and that was to give away free equipment, to give away advertising and promotion, and to give away, in some cases, cash to secure my accounts. On that basis, I had a very difficult time competing.

My company is small and I am not capitalized to provide free equipment. No banker or lending institution in his right mind would loan me that type of money, because the return on investment for such a loan is just not there.

September 1 of this year was kind of the straw that broke the camel's back. I lost my last large Coca-Cola account. And this account at its height had been $10,000 a month.

It is down to zero now. At that point I decided I am no longer in the soft drink business. I cannot compete on this basis and I will no longer try to go on with it. What I am trying to do is to diversify in other areas and survive in my business.

If Congress sees fit to pass the bill that you graciously introduced, I may have the option to reenter this market if I am still around, and if I can compete on a fair and equal basis. If they do not, I will not have that option.

There is a definition of insanity that I have heard which is "doing the same thing over and over again expecting a different result." I no longer am going to engage in this insanity. I cannot.

As much as I dearly love this business, it is just not feasible for me to stay in the soft drink business as it exists today.

I think that in my marketplace, the consumer on level A being my customer and the consumer on level B being the person that ultimately drinks the soft drinks, will be paying a dear price at some time.

I really honestly believe that, the independent people, such as Mr. Jason and myself, and a number of other people in this room, keep a check on the outrageous profitability of the soft drink purveyors.

We are in business to make a profit, we are not necessarily in business to make an outrageous profit. We keep that in check and balance. I think the market will miss us.

I am not here to suggest that there is any type of conspiracy. I too feel like I am caught in the middle of it. But the net effect of what happened to me and what is happening to other people is the same as if there were a conspiracy.

And so what I would plea on my own behalf, and on behalf of my colleagues that are still in the soft drink business, is that Congress consider passing the bill which will make treatment of everybody in the marketplace fair and equal. And I sincerely thank you for listening.

[The statement and questions and answers follow:]

STATEMENT OF DOUGLAS S. DAMON

Mr. Chairman, my name is Douglas S. Damon. I am president of Damon Distributing Company and I am appearing here today in support of S. 2347.

Damon Distributing Company is located in Sparks, Nevada. We have been in the business of manufacturing syrup concentrates for many years. We were, until Coca-Cola and Pepsi-Cola began giving away dispensing equipment, also in the business of selling, leasing and renting fountain equipment that dispenses soft drinks.

We have not placed a lease or sold a complete dispensing unit in five years. Why should a customer spend money on equipment when he can have Coca-Cola or Pepsi-Cola place not only soft drink equipment, but also ice makers, liquor equipment, vending machines, advertising materials, beer equipment, and yes, even cash up front. The bottling companies do not make a profit when they present these programs, but they are able to garner massive infusions of cash from other departments. They chalk up the losses to advertising and promotion. We have to make a profit. When we are gone, does anybody suppose that Coke and Pepsi are not going to one day decide to become profitable in these areas. If they do, who is going to restrict the potentially excessive levels of profitability? It won't be companies like mine because we will be out of business.

Because I cannot afford to loan equipment, I have seen a steady deterioration in my syrup sales. If Coke and Pepsi provide equipment they demand that the customer use their respective syrup products. This locks me out. I have had to diversify or die. The road has not been an easy one.

Regrettably, on September 1st of this year, I was notified by a large casino account at Lake Tahoe, Nevada, that all of their soft drink syrups would henceforth be procured from the Coca-Cola Bottler. We had enjoyed that business for 15 years. This changeover has proved to be the final chapter to a story that has been going on for years, but intensified about three years ago. I am now effectively out of the Coca-Cola business. This loss was the proverbial "straw that broke the camel's back."

The account to which I refer was at its height a $10,000 per month syrup account. Why did I lose the account? It was not because of poor service. The account's people will admit that our service department's performance was exemplary. It was not because of the price of the syrup product. Our prices were as much as 25 percent lower. Very simply put, it was because we would not install and loan beverage dispensing equipment at no charge. Nor would we provide additional monies, called transitional allowances, to keep the account. From a return on investment standpoint, it did not make sense to me. The cost of the equipment was too great and the return, too small.

My market area contains a small population base of less than 500,000 people, but includes a significant number of large volume accounts that attract significant numbers of customers—i.e. casinos and ski resorts.

Traditionally, we were favored with a fair proportion of the casino business. We were so favored because we specialized in the service of their dispensing equipment to a greater degree than the bottlers and because we manufactured our own line of quality syrups that were favorably priced over our competitor's products. For a number of years, we maintained our competitive edge in these accounts. A typical scenario to secure a casino account would be to sell Coca-Cola products at or near cost and our own flavor line at a price that generated a reasonable profit. Under normal circumstances Coca-Cola and Pepsi-Cola could not match our own flavors in price so we were able to maintain a precarious balance in the marketplace. Then, the "cola wars" began to intensify.

Coca-Cola and Pepsi, in the course of battling each other, stumbled across my Achilles heel. Very simply, they found that if they loaned equipment to the account at no charge (all paper maneuvering and accounting extrapolations aside) they could displace me as that account's vendor. Once the bottlers found that my accounts, for cash flow reasons, were willing to pay more money for product in the long run to preserve short term cash flow, their efforts to displace us as suppliers were relentless. The end results were predictably disastrous for me. Within a year, my soft drink syrup base in the casino market was decimated. My soft drink share of business has been decreased about $50,000 per month or about fifty percent of my total business.

You may ask the question, why don't I loan equipment to the account as the bottlers do. The reason I don't is twofold. First, I am a small company that does not have the capital reserves to lay out as much as $50,000 in free equipment to secure a large account. I could not even comfortably lay out $1,000 to outfit a small cocktail lounge with free equipment and justify the outlay in terms of reasonable return on investment. Second, no monied individual or banking firm is going to capitalize me so that I can loan the equipment on an equal footing with Coke and Pepsi. The reason these lending institutions won't capitalize is that the return on investment is simply not there. This brings me to a point and I believe it is a very important point. The bottlers do not seem to think that at this juncture they have to be profitable in their syrup business. Many of them are not profitable now, but can afford to wait. As post mix syrup takes a greater share of soft drink sales, those non profitable post mix syrup operators are guaranteed to become profitable. This will become very easy without companies such as mine in every market. Who, then, is going to suffer. I submit to you that it will be the consumer. Until recently, us "little fella's" have been a great check on the giants in most markets.

It goes without saying that to sell, lease, or rent beverage dispensing equipment in my market is a business opportunity that I have not enjoyed for a number of years. Coke and Pepsi are even going after the small tavern accounts with their free equipment now. Such a course cannot be financially justified and is blatantly unfair.

I have seen instances where the bottlers provide non dispensing equipment to secure accounts. I know of several accounts that I lost that have total gross syrup sales of $200 per month or less where the Pepsi bottler placed ice makers at no charge with a value in excess of $1,000. Find me an accountant who could justify that free placement in terms of reasonable return on investment.

One of my customers recently told me that representatives of one of the bottlers said that they would provide whatever was necessary in equipment and transitional

funds to secure the syrup business. We continue to serve that account because the bottler will not service the liquor equipment, coffee equipment, and orange equipment as our company does. There is historical precedent that prices rise when competition stops. When we lose the small independents, the checks and balances will be gone. Coke sets the pricing and Pepsi follows. If legislation is passed to allow us to compete fairly, the consumer will continue to benefit. If not he will pay a higher price.

The Coca Cola Enterprise (company owned) Bottlers have either pulled out of the syrup business or have dictated that all syrup operations operate profitably. The accounts in these companies came to the conclusion, and I believe it is a wise conclusion, that every operation in a company should generate a profit. We have been trying to tell them that for years. The shift in attitude of Coca-Cola Enterprises says something very significant about the unfair trade practices that have existed for many years and still exist, unfortunately, throughout the industry.

I am not here to suggest that Coke and Pepsi have conspired to drive the independents out of business, but I do suggest that the policies of equiment give aways have had the same net result as if there was indeed a conspiracy.

Sadly, it is too late for Congressional action to salvage my soft drink business. At the present time, I am struggling to save my business by diversifying into different areas such as juice concentrate manufacturing and related equipment placement. One definition of insanity is "doing the same thing over and over again expecting a different result." I will not continue to fight the Coca-Cola and Pepsi equipment give away program under the present conditions. If Congress and the President will allow me to compete fairly, I will then have the option of re-entering the soft drink syrup and equipment business. If not, I will try to rebuild my business in another direction and hopefully survive.

As a closing thought, if it is the intention of this Congress to allow Coca-Cola and Pepsi to totally control the soft drink business to the virtual exclusion of every other manufacturer then no action is necessary. If on the other hand, it is the intention of Congress to allow the small businessman and the entrepreneurial spirit to flourish, then enact legislation that will enable us to compete fairly and equally by prohibiting the giants from giving away equipment solely to enhance their control of the market. If you do the consumer will be the ultimate beneficiary.

Thank you.

QUESTIONS OF SENATOR GORE AND THE ANSWERS THERETO

Question 1. When you were in the business of renting fountain equipment did your rental agreements with your customers require the purchase of any of your syrup?

Answer 1. No, we do not require purchase of our syrups. It has been a number of years since we have been able to rent fountain equipment as it has been loaned to even the smallest of accounts for years in my market. Our marketing philosophy would be to secure a rental and to sell the product separately. This would give us the opportunity to garner two separate and distinct accounts. The absence of one would not preclude the other.

Question 2. What was the normal term of your rental agreements with your customers for fountain equipment? Could those agreements be terminated at will by either party, or was there a contractual agreement for a particular time period?

Answer 2. The terms of our contracts were normally four years. They could not be terminated by either party under normal circumstances.

Question 3. Based on your experience, when the syrup companies loan equipment for free or at a reduced price do they always require the recipient to buy a certain kind of syrup? When purchases of syrup are required, must the purchases be made directly from the syrup company, or can the recipient of the equipment buy syrup from an independent wholesaler?

Answer 3. My experience shows that the Coca-Cola and Pepsi-Cola bottlers absolutely and unequivocably require that syrup be purchased from them when they loan equipment. The independent wholesaler is totally locked out in my market.

Question 4. Are You aware of any independent syrup wholesalers that loan equipment for free or at a reduced price?

Answer 4. I am not aware of any independent wholesaler in my market that loans carbonated beverage dispensing equipment. In most instances the numbers do not make sense to do so.

Question 5. If S. 2347 is passed, will that result in higher overall costs for fountain beverages to retailers, particularly restaurants and taverns? If so, are those increased costs likely to be passed on to the retailers' customers?

Answer 5. I believe that if S. 2347 is passed beverage prices will be lowered to retailers. As an example, my price today would be $20.00 (list street price) for syrup in 5 gallon containers as opposed to $28.50 from the bottlers (list street price). The equipment rental would in no way gobble up this difference as a typical fast food account will use at least 20 5 gallon containers per month. I believe that what the consumer will be ultimately faced with is significantly higher prices with us not around. We independents keep a check and balance on the gouging of syrup prices. If you don't believe that look to those areas such as Utah and Oregon where there are no independents. The markets are dominated by premix products in those areas. That product is 350%+ more expensive than the post mix syrup that we offer. The trend in our industry has been for a greater percentage of the market to purchase syrup. This trend will continue. For the bottlers to maintain their present levels of profitability, they will have to sell their post mix syrup for $75.00 (instead of $28.50). Without us independents to stop this gouging, the Coca-Cola and Pepsi-Cola Bottlers will easily be able to arrive at these high pricing levels. With us, they will never be able to do so. I submit that the consumer will be devastatingly impacted if S. 2347 is not passed.

Question 6. Do both Coke and Pepsi invest in research and development of fountain equipment? If so, in your judgment is that an element of competition between Coke and Pepsi? Could S. 2347 reduce that competition?

Answer 6. Yes, Coke and Pepsi do invest in research and development of equipment. This is an element of competition and is brought in large part by the efforts of the independent who by their service orientation require that Coke and Pepsi are always "on their toes" equipment wise. The passage of S. 2347 would ensure that this competition will continue.

Senator INOUYE. So you consider this to be unfair competition?

Mr. DAMON. Well, I consider it a lot of things. That is one of them, unfair competition. I consider it ultimately not in the best interests of the consumer.

Senator INOUYE. You spoke of the giving of cash and free advertising. Can you elaborate on this?

Mr. DAMON. The fancier term that I have heard used for this is transitional allowances.

As an example, you own three restaurants. You own a chain of small restaurants. Up front marketing funds, or transitional allowances, I have seen paid to the accounts in significant numbers, based upon gallonage figures. Paid up front to the people.

This has the pretense of being a marketing scheme. Actually it is just to me handing cash over to somebody to pick up his account. I do not know how other people would describe it, but that is how I describe it.

Senator INOUYE. What about free advertising?

Mr. DAMON. As I understand, the major bottlers get funds off of all the soda that they sell, be it in cans and bottles or in the syrup form like we do. They get so much money back, I think it may be a nickel a gallon, or whatever.

These funds can only be spent on advertising and these funds are not always available to us. That is why you will see expensive clocks and expensive neon signs on small mom and pop stores, and so forth.

It comes out of these funds. Menu boards, a lot of different programs that are not available to people such as myself who are not in the Coca-Cola marketing program or a Pepsi-Cola program.

Senator INOUYE. How many large bottlers are involved in this type of activity? And who are they?

Mr. DAMON. I have no idea how many bottlers there would be involved in that. But I would say all of them are. One hundred percent would be involved in the advertising.

Senator INOUYE. Mr. Jason, as you indicated, Pepsi-Cola and Coca-Cola have been involved. Are there any other companies? Or just those two?

Mr. JASON. Relative to advertising?

Senator INOUYE. The unfair competition that you have been complaining of.

Mr. JASON. We have not experienced in our marketplace any other major soft drink manufacturers involved in the types of programs that we have seen in our market specifically with Pepsi-Cola, and to a smaller extent with Coca-Cola.

No, we do not see that with RC Cola, we do not see it with 7 Up or Sunkist or Canada Dry. As a matter of fact, as a Sunkist distributor, if there are marketing funds available, they are paid to the wholesaler, who then has the opportunity to try and use those dollars to increase sales of their product in the account. They do not go directly to the user.

Mr. DAMON. If I might clarify, yes, I would agree with that. I thought you meant bottler on the local level. To my knowledge, Coke and Pepsi are the major ones.

Senator INOUYE. Thank you very much, Mr. Damon. Ms. Lippy.

STATEMENT OF LORETTA LIPPY, NATIONAL LICENSED BEVERAGE ASSOCIATION

Ms. LIPPY. Hello. My name is Loretta Lippy, and I thank you for the opportunity to appear before you and the Members of this subcommittee.

I am the Eastern Vice President and a member of the Legislative Committee for the National Licensed Beverage Association, NLBA, representing the retail alcohol beverage industry in bars, taverns, cocktail lounges and restaurants around the country.

I am also an officer of the Pennsylvania Licensed Beverage Association. My husband and I are co-owners of the Valley Tavern in Seven Valleys, Pennsylvania. And I am accompanied today by John Chwat of Chwat/Weigend Associates, the Washington representative from the NLBA.

The NLBA and its thousands of members around the country are opposed to the passage of S. 2347, which seeks to amend the Federal Trade Commission Act to prohibit certain unfair practices by soft drink manufacturers on the distribution of beverage dispensing equipment to retailers.

Mr. Chairman, contrary to contentions of the supporters of this legislation, placing soft drink beverage dispensing equipment in a tavern for no charge, or at a negligible charge, does not create an obligation to purchase the soft drink syrup from the company giving away the equipment.

This is just not the case. And is contrary to our retailer business practices. Let me use our tavern as an example.

Our Valley Tavern purchases our soft drink dispensing equipment. We did not receive it for free, or pay a nominal fee, or lease the equipment. We bought it with our hard-earned money. And as

far as a give-away program, NLBA believes many of their retailer members purchased these types of equipment.

While we have no industry-wide study to detail how many of the over 600,000 retailers of the alcohol beverages around the country either purchase or receive free soft drink beverage dispensing equipment, this practice is an acceptable, normal course of doing business in today's economic environment.

Despite our tavern's choice to purchase these units, NLBA believes free distribution is not wrong. We understand that other retail industries receive free products from their suppliers for promotional or marketing use that S. 2347 would seek to eliminate.

NLBA is also opposed to this legislation for a variety of other reasons. First of all, consumer demand from our tavern customers determines the type of soda or product mix we purchase for our businesses.

Would it not be deceptive consumer practices, or trademark violations, for a retailer to have a dispensing unit with, say for example, Coke on the outside and then purchase an inferior or other brand of soda syrup product merely to save a few cents?

It is unfair to impose on retailers the restrictive provisions founds in S. 2347, prohibiting inducements such as accepting signs, supplies, money, services or other things of more than nominal value.

What the proponents of the bill ignore is the common practice of a soft drink supplier to assist his tavern owner or retailer in deciding what types of equipment to have in his or her establishment.

It is the soft drink supplier who undertakes the research and development on improving outdated soft drink dispensing equipment. It is the soft drink supplier who keeps abreast of new technological advances in equipment and informs the retailer on the best competitive mix of equipment for their establishment.

There is no need to change this long-established relationship through S. 2347 between our retailer and their soft drink suppliers.

Finally, S. 2347 claims to protect competition within the soft drink dispensing equipment market. To the contrary, by eliminating supplier marketing and promotional support to the retailer, it will reduce profits and hurt retailers.

The real victim of this soft drink dispensing battle is the customer. We believe that this is special interest legislation, pure and simple. It is unnecessary, and we therefore urge this subcommittee, the full Committee and the Congress to reject S. 2347 and not to report the bill out for final consideration. Thank you.

Senator INOUYE. Thank you very much, Ms. Lippy. You have indicated that you purchase your equipment?

Ms. LIPPY. Yes, we do.

Senator INOUYE. Have you ever been offered free equipment?

Ms. LIPPY. No, we have not. If I may along that same vein also say that I do know that some small establishments, when they first start out, are perhaps offered and maybe repay in loan.

My husband and I have been in business for 22 years and we saw fit three and a half years ago to buy our own system, and choose what sodas we wanted to put on.

Senator INOUYE. No one has ever offered you these special inducements?

Ms. LIPPY. Not for soda, no.

Senator INOUYE. And you indicated that it would be less than honest if you had a Coca-Cola sign and served something other than Coke?

Ms. LIPPY. Absolutely. And I am sure these things happen in some instances, because I know of no contractual agreement, that if someone puts the equipment in you must continue to sell their soda.

Senator INOUYE. So you are indicating that your sale would depend upon consumer preference?

Ms. LIPPY. Yes. And I have to be honest and say also price. I like to be able to buy at what I consider the best price for the best product. Or a comparable product.

Senator INOUYE. So if your customers preferred Coca-Cola, and a Coca-Cola representative came over and offered you equipment at a very nominal amount, would you accept it?

Ms. LIPPY. I doubt that I would. But I have to say that I do not know what all the other establishments would do.

Having been in the business for as many years as we have been, and being established, we do not care to do it. But we do sympathize with the new businesses coming into being today.

Senator INOUYE. The words in this bill are quite similar to provisions that we find in a current law, the Federal Alcohol Administration Act.

Ms. LIPPY. I am very familiar with that, sir.

Senator INOUYE. In that act it is illegal in the industry to offer inducements such as free dispensing equipment, if those inducements would exclude the sale of other brands.

And the language in this bill is quite similar to that. Would you object to that type of language in this bill?

Ms. LIPPY. I would have to take that back to my board of directors for consideration. But being from Pennsylvania, we are very restricted with the beverage alcohol products, and what we can or cannot do in addition to what the BATF also tells us.

Senator INOUYE. Do you believe that the language found in the Federal Alcohol Administration Act to be unfair and against competition?

Ms. LIPPY. I have mixed emotions on that. As I said, we have been in business a long time. And I think there are times when it would be enabling to a small business to have that helping hand, whether it be from a soda company or a beer company, or perhaps another manufacturer of ice cream or anything.

Senator INOUYE. Senator McCain?

Senator MCCAIN. Thank you, Mr. Chairman. Mr. Jason, is it your view that large syrup suppliers are trying to drive you out of business?

Mr. JASON. No, it is not. It is my view that the large syrup suppliers are trying to compete for the number one position in the marketplace.

They will do just about anything they have to do to get there, and we are in the middle. It is a squeeze play. And frankly while it is not intentional, we believe it is not intentional to drive us out of business, we feel that it is inevitable.

Senator McCAIN. Mr. Damon, if this legislation is enacted, in your view, what impact would it have on the price of soft drinks?

Mr. DAMON. I would say, and this is opinion, it is hard to foresee something like that, but I would say that it would stabilize them. It will keep them at the levels they are now.

The best example I can think of as to the possibilities would be if you take what a bottler sells, a case of 24 12-ounce cans now, say $6 at a wholesale level, and his costs are somewhere around $2.

If you were to apply those same numbers of profitability onto the syrup you would be looking at syrup in the neighborhood of $75 a gallon rather that $25 a gallon as it is now.

Without the checks and balances I talked about earlier of us type of guys around, I think very well that something like that would be conceivable, because more of the soft drink business is going the route of the syrup sale.

Senator McCAIN. Ms. Lippy, in your personal opinion, what would happen to small restaurants that dispense soft drinks, in the event this legislation were enacted?

Ms. LIPPY. I would think that it would hinder, and here again I am going to say very small and also new ownership coming into being, to enable them to even serve post-mix, thereby having to handle the bulk of cans or bottles, which is not as profitable.

Senator McCAIN. Thank you very much. Thank you, Mr. Chairman.

Senator INOUYE. Thank you. And thank you very much. The next panel is Mr. Sanford Hahn, President, Perfection Equipment, and Mr. Alfred Griggs from Coca-Cola of Northhampton, representing the National Soft Drink Association, and the Vice President of Dr Pepper Company, Mr. James W. Watkins.

STATEMENT OF SANFORD HAHN, PRESIDENT, PERFECTION EQUIPMENT

Mr. HAHN. Mr. Chairman, I am Sanford Hahn. I am President of Perfection Equipment Company of Gurney, Illinois, which is in the metropolitan Chicago area.

And I would like to thank you for this opportunity to present my entrepreneurial viewpoint and make particular reference and thank you for your insight into understanding and perceiving this problem as recited in your Senate bill 2347.

Perfection Equipment Company is an original equipment manufacturer, and that is we make the unit that makes the soda water that is mixed with the syrup. So we really only make a piece of hardware. But that piece of hardware is commonly referred to as a carbonator.

Now, our carbonator is quite unique in that back in the late 1960s and early 1970s we achieved technological expertise in the art of fluidic technology. And our patents that we received in the areas of refrigeration and carbonation are unique to Perfection.

And the end result is a piece of equipment that carbonates the water to perfection and also refrigerates it in an environment indicative and reflected by the patents. So this magic box really takes potable water, carbonates it, refrigerates it, recirculates it

many hundreds of feet, brings it back and recarbonates it and rerefrigerates it.

This is not a piece of equipment that you will find in Ms. Lippy's bar generally. It is something that you will find in the Senate cafeteria, dispensing soda water, which I believe is Perfection. And the larger projects, those indicative of the new large projects in both Maui and Hawaii Kaloa, as well as the main island of Hawaii.

It is these projects which require this state-of-the-art sophistication that reflect a level of necessity for engineering. A great deal of planning, if you will, has to go into a project like a Hyatt on Hawaii Kaloa, like a Smithsonian Institute Air & Space Museum, like many hundreds of major facilities, Heinz Auditorium in Boston.

These projects are generated through architects. The architect has a space to plan. The architect then goes to what is commonly referred to as a food facilities consultant.

There are about 400 in the United States that specialize in supporting the architect who has this project, whose sole responsibility it is to design the food facility and specify equipment.

We have probably 85 percent market penetration in the area of specified equipment for planned food facilities in the area of carbonation.

So when an architect and a consultant get together and they design a facility, they will very often send the prints, the plans for the facility, to Perfection. Our engineering department then sizes it and designs what is commonly referred to as a conduit routing.

Because that magic box that we invented back there in late 1969 is put in a room many hundreds of feet, in most cases, from the point of beverage dispensing, for various reasons.

It is a compressor and it could make noise, and it needs air to breathe. So you cannot put it out there in the cafeteria line or whatever. It has to be remoted.

So this all has to be designed into an overall concept. That concept is then generated and plans are submitted to a kitchen equipment contractor, who will bid on that project. There may be three or four of them out there, maybe 10 of them.

They all ask us for pricing. Meanwhile, we have generated these plans. We have spent a lot of time and effort in engineering time, going back and forth on the phone and finalizing it, and the specification is written.

We then submit a price. That price is then given to the contractor, and the contractor may very well send us an order. He usually does.

Unfortunately, we have found here of late, and we have been able to beat the give-away program until just recently, the last three or four years, we had a state-of-the-art technology that the syrup companies generally could not compete with because they did not have the equipment or were not interested in getting into a confusing set of situations like an engineered project.

So what we did is get along pretty well. Then up pops the devil and there are immense give-away programs, and especially in the metropolitan areas, such as Washington, D.C.

A typical example, how we are really hurt by Coca-Cola and Pepsi-Cola, depending upon the area of the country and how much marketing funds they have to spend, is Smithsonian Air & Space.

I have a list here, too numerous to mention at this time, but one in particular being the Smithsonian, we had quoted and budgeted $78,000 for the beverage dispensing equipment. And it was engineered around a design concept.

That got shot down just the minute that Mr. Coke walked in the door, because in this instance it was Co Cola. And it was taken out of the project, other equipment was put in, a lot of redesign had to be done, a lot of unnecessary expense.

And I had a comment just last week of all the problems they have had, not related to the equipment they put in but rather the problems they had getting the equipment in. This is one set of circumstances that has enumerated itself with more frequency of late.

And consequently I feel there is a great injustice done by the major syrup companies who intend to be number one and compete with each other by virtue of unfair business practices and unfair tactics. And this is really the tip of the iceberg. And thank you very much.

[The statement and questions and answers follow:]

STATEMENT OF SANFORD A. HAHN

Mr. Chairman, my name is Sanford A. Hahn, and I am President of Perfection Equipment Inc. of Gurnee, Illinois. Perfection Equipment was incorporated in 1964 with two employees and one thousand square feet to operate. In 1979 I became president and chief operating officer. We currently have twenty-two employees and fifteen thousand square feet for manufacturing and administration. Perfection invented and acquired patents in the field of fluidics technology as it relates to refrigeration and the carbonating of water.

Since the early 70's we have been developing marketing programs which carry our unique patented engineering concepts to the planned food facility designers, commonly referred to as food facility consultants. It is the job of these consultants to formulate proper engineering concepts and design criteria for individual applications relative to food service.

SOURCE OF SALES

As director of sales and marketing I have established a network of manufacturers representatives throughout the continental United States. These agents, along with myself, distribute catalogs and make presentations to food service consultants and major chains, such as hotels, fast food and institutional feeding facilities. Another means of reaching potential customers is various and international and regional industry trade shows. Perfection's target is the food service consultants, in that 85 percent of our sales originate by virtue of written specifications prepared by these consultants designating Perfection as the equipment to be supplied on the project.

Perfection's product, being a complete beverage system, includes a refrigerated recirculating carbonator, varying quantities and descriptions of dispensers, a choice of racks to house the carbonator and syrups and the necessary insulated beverage tubing to deliver the carbonated water and syrups from a designated equipment room where the carbonator is located to various points of dispensing as determined by the customer. Thus each beverage system is custom fabricated relative to volume required and design criteria.

A typical project starts with preliminary drawings prepared by a food service consultant and is forwarded to our engineering department to make recommendations for horsepower sizing, componentry selection and budget estimate. A further step is for Perfection to prepare suggested specifications and recommended conduit routing. The conduit plan is a designated routing for the beverage lines to run from the carbonator to various points of dispensing. Site inspections and mechanical trades meetings are often required to properly engineer a complicated multistation project. The man hours and expenses are incredibly costly, especially if one or more site visits are required.

The food service consultant will incorporate the beverage portion, designating Perfection Equipment as the manufacturer/supplier, along with other kitchen equipment required for a project and issue drawings and written specifications to several kitchen equipment contractors (KEC'S). The KEC'S will contact Perfection for a formal proposal to furnish, install and warrant the beverage equipment as specified. These duplicate inquiries may come from one or as many as a dozen KEC'S. The KEC'S will prepare bids for the total equipment package including the beverage system(s). At this point the major portion of our work is done. To *furnish, install* and *warrant* the beverage systems is the *profitable* aspect of each job.

Senate Bill 2347 seeks to eliminate equipment give-aways by the two major syrup suppliers. Let me explain how the Coke and Pepsi give-away program hurts not only my company but others as well. It is common practice for a syrup company representative to go to an owner of a food facility, in the course of negotiating a price for syrup products, and often free equipment to dispense their syrups. Often this is done without regard for what was planned or engineered by the designer. An owner or operator of such a facility may very well incur costs he is unaware of by virtue of additional mechanical requirements (such as additional conduit, changing electrical and/or plumbing and possible addition of cold plates) necessitated by the installation of free equipment.

At this stage of the design process my company could have incurred costs as high as several thousand dollars for engineering, conduit plans and site inspections. There is no way to recover these spent dollars. A sale could be lost at this point or as late as material being delivered on site and a cancellation order is given to my company by the owner, with the syrup company representative (Coke or Pepsi) sitting at his side holding a contract to furnish all beverage systems at no charge as long as they are the *exclusive* supplier of the syrup products. Keep in mind, this is not limited to Perfection Equipment, other beverage equipment manufacturers also lose contracts at the eleventh hour.

Specifically some of our recent lost projects include the following:

Smithsonian (Museum of Air & Space) Washington, D.C. Lost after formal quotations were prepared and sent to the various kitchen equipment contractors bidding the project. Bid amount $78,024.

Eastern Michigan University, Ypsilanti, Michigan. Lost after bids were submitted. Bid amount $42,184.

Sheraton Cypress Hotel, Fort Lauderdale, Florida. Lost after receipt of purchase order and partially fabricated. Bid amount $31,306.

Princess Hote, Scottsdale, Arizona. Lost after Perfection received a purchase order from the awarded KEC. Bid amount $5,360.

Connor Prairie Museum, Noblesville, Indiana. Lost after receipt of purchase order and partially fabricated. Bid amount $11,798.

Hughes Research Bldg. #254, Malibu, California. Lost after material shipment. Bid amount $8,372.

Penrod's, Miami Beach, Florida. Lost after lengthy engineering preparation and two field meetings. Bid amount $141,629.

Known Lost Sales (4/88 through 9/88) to Equipment GIVE-AWAY Total $247,473.

It is outrageous that approximately twenty-five percent of our potential sales are lost to the equipment give-away program offered by the two major syrup vendors, after the equipment of only my company has been expressly designated in the contract specifications. As a manufacturer of equipment, we attempt to sell a product that is competitively priced and engineered for the application. The essence of competition and good business practice cannot offset an opponent who is giving away a product that we must sell to exist. I feel it is an unfair inducement for the syrup companies to be allowed to give-away equipment to get their syrups sold, and maneuver themselves into a situation where they can ultimately manipulate the price of their primary product—syrup.

PERFECTION EQUIPMENT, INC.,
Gurnee, IL, October 24, 1988.

Senator ALBERT GORE, Jr.,
Chairman, Consumer Subcommittee, U.S. Senate,
Committee on Commerce, Science, and Transportation, Washington, DC.

Re: Your letter dated October 13, 1988. Senate Bill 2347.

DEAR SENATOR GORE: Thank you for your continued interest in Senate Bill 2347 and your sincere efforts to address an ongoing problem that effects thousands of independent manufacturers, distributors of equipment, installers and service agencies,

as well as, other medium to small size syrup companies who are precluded from doing business as a result of Coca Cola and Pepsi Cola Companies marketing tactics.

Question 1. I understand that your business is primarily the design and sale of large-scale beverage systems, and that you have lost several customers because Coke or Pepsi has agreed to provide equipment to those customers for free or very low cost. Have you ever marketed your product to Coke or Pepsi for use in their free or reduced price equipment programs? If not, why not? If so, what was the result?

Relative to your Question #1 heretofore, the major syrup companies generally limited their equipment Give-Away Program to what is commonly referred to as top of the counter dispensers. Those units generally operate in moderate volume cafeteria operations, snack shops and restaurants. Perfection Equipment does not manufacture a counter dispenser. Perfection's type of equipment is referred to in the industry, as remote, in that the power pack is almost always remoted from the point of dispersing and usually supplies more than one beverage dispensing stations. Up until the last two years the Give-Away Program had little to no effect on Perfection's type of projects. The fact that Perfection Equipment has its own factory trained installation and service personnel there was no need to attempt marketing through the major syrup suppliers. Furthermore, since our patented technology is so vastly different from what the syrup companies are accustomed to, it would take an immense effort in resources of finance, manpower and years to acquaint and train the different syrup companies buying sources. It is just not in the cards for a small company to attempt to market an item which is used in maybe five percent of the syrup company's Give-away projects. Not withstanding it is conservatively estimated that Perfection Equipment loses at least $500,000 in sales per year to the Give-Away Program.

Question 2. Do you have any information to suggest that either Coke or Pepsi manufacture their own fountain or beverage dispensing equipment? If they do not, where do they obtain the equipment they provide for free or at low cost? Wouldn't they have to purchase it from Independent equipment manufacturers or wholesalers?

Relative to Question #2, it is my understanding that neither Coke nor Pepsi manufactures any type of equipment that Perfection manufactures. The syrup companies do, however, have certain patents or copyrights relating to their company identified beverage dispensing valve, i.e. the Dole Valve is in reality a valve purchased exclusively by the Coca Cola Company and is manufactured by the Dole Valve Company under a license agreement. It is further my understanding a purchase of valves and/or replacement parts can only be acquired through the Coca Cola Company. The syrup companies buy rudimentary equipment from three or four independent manufacturers. The manufacturers they choose depend on what division, at what syrup company, in what area of the country, for a particular application. One of the largest of these suppliers is the Multiplex Company of St. Louis, Missouri, who has been in business for over fifty years. Multiplex has taken a position relative to Senate Bill 2347 and I am enclosing herewith for your reference, a statement by the president of the company. It is also noteworthy that not only does he wholeheartedly support the bill, he and his company have just recently become the recipient of a presidential citation for excellence. Again, the acquisition of equipment from independent manufacturers generally does not include the type of equipment we manufacture. When the occasion arises that our type of equipment is required, the syrup suppliers go to one of their regular independents and attempt to get something close to what is needed without regard to what has already been specified and designed. The trusting operator of the facility thinks because he is dealing with a major syrup company and he is "Getting It Free" the operator accepts it on face value. What the deal does is preclude ease of installation, high quality performance levels, independent union trades installations, subsequent independent service and equally important the customer's choice of products other than product availability dictated by either Coke or Pepsi.

Question 3. If Coke or Pepsi do purchase equipment from independent manufacturers or wholesalers, how do they select those suppliers? Are you aware of any particular specifications or requirements they impose on their suppliers?

Relative to Question #3, I partially answered this in the previous paragraphs and while there is in fact alleged standards by the syrup companies of all types of beverage dispensing equipment and componentry, more standard is politics and longevity which dictates acceptance by the parent companies. A prime example of this would be the horror story often told by Mark Chudnow of the Chudnow Company of New York, who is a large manufacturer of stainless steel fittings, regulators and gauges for the beverage dispensing industry. With this communique I will be asking Mark to relate his story to your office in the near future for the record. Bottom line, he

has been trying for over twenty years to be accepted by the Coca Cola Company and after much frustration has yet to have any satisfaction.

Question 4. You testified at the hearing that the equipment furnished by Coke for the Smithsonian account you lost was not of similar high technology to your equipment. Is this typically true of the equipment furnished by Coke or Pepsi? If your equipment is of better quality and higher technology, do you know why Coke or Pepsi does not purchase and use it?

With reference to Question #4, there is no doubt the technology utilized in the Smithsonian application is not the high standard of Perfection by virtue of our patented features which provide for colder temperatures and the highest maximum level of carbonation. Yes, this is typically true of Coke and Pepsi. A good analogy would be when we are precluded from installing our equipment which is a refrigerated system, the syrup company will furnish a system referred to as an ice-cooled system. This could be compared to you going out to buy a new electric refrigerator and instead come home with an ice box. Obviously, the technologies and results are different, but the price is right. Again, the primary reason for Coke or Pepsi not participating with our equipment lies in the fact that they deal with others on a regular basis, our price is somewhat higher and they would have to train people to understand our technology.

Question 5. If S. 2347 is passed, in your judgment will it result in higher costs for fountain beverages to retailers, particularly restaurants and taverns? If so, are those costs likely to be passed on to the consumer?

Relative to Question #5, if Senate Bill 2347 is passed we would be creating a true competitive market for all syrup companies to compete on an equal basis. I believe you will see syrup prices come down because the major syrup companies will no longer have the capital investment of millions of dollars which is reflected on their balance sheet as a cost of doing business. You would eliminate the monopoly of Coke and Pepsi by allowing Dr Pepper, 7 Up, RC Cola, etc. to compete without being intimidated by the major syrup companies domination by Give-Aways. I would hope to equate the passing of this bill to the deregulation of the airlines. I truly feel as a consumer we all benefit from a free competitive marketplace.

Sincerely,

SANFORD A. HAHN,
President, Perfection Equipment Inc.

Senator INOUYE. You just testified that your cost was $78,000 for the Smithsonian?

Mr. HAHN. That is correct.

Senator INOUYE. Was the Coca-Cola price just as high?

Mr. HAHN. Well, it is my understanding that there was no charge.

Senator INOUYE. No charge?

Mr. HAHN. That is correct.

Senator INOUYE. Was the equipment of similar high technology?

Mr. HAHN. No, sir.

Senator INOUYE. Do you mean to say that Coca-Cola offered Smithsonian equipment at no cost?

Mr. HAHN. I would say that they do that. I hear stories, I do not know, because I am not there in the marketing department.

But I hear stories from the people who receive the equipment, representatives you see, and when you deal with projects of this size you are generally dealing with what is termed a concessionaire.

A concessionaire might be ARA, which is a very large concessionaire in the Philadelphia area. Actually they are worldwide. They were the concessionaire for the United States Olympics.

Very often as a matter of routine policy a major beverage company, be it Coca-Cola or Pepsi-Cola, will supply all the carbonating beverage equipment for those people in a given project. Almost always.

Senator INOUYE. Will your equipment handle Coca-Cola and Pepsi-Cola?

Mr. HAHN. Oh, yes sir. Our equipment carbonates water and can be mixed with anybody's syrup.

Senator INOUYE. Then why should Coca-Cola be insisting on putting their equipment, if your equipment can handle Coke?

Mr. HAHN. It does not make sense, and that is why I thank you for this opportunity to be heard.

Over and over again we asked them that question, and we asked both Coca-Cola and Pepsi-Cola that question. And they say, it is the other guy's fault, because I have to give it to get the business.

They say that about each other, and it is like, you know, there is mass confusion as to a logical answer for why a major syrup company who spends millions, millions of dollars on a give-away program, it just does not make sense to spend this money unnecessarily, when in fact they purportedly both stand ready to not give equipment.

I mean, I hear that from them. But I do not see it happening. As a matter of fact, I would like to make a little aside here. I have a resume that was sent to me by a district manager of the Coca-Cola Company, who is now looking for a job. I would like to read from that resume, if I may.

In one of this salient points to sell himself he said, "insured first year capital equipment cost savings of $400,000 by negotiating the elimination of companies furnished dispensing equipment. '

So he made his mark with his company during his tenure there by eliminating it.

Senator INOUYE. You have suggested that this practice that you have described is inconsistent with competition.

Mr. HAHN. Yes, sir.

Senator INOUYE. However, those who are opposed to this measure suggest that it is highly competitive. What do you say?

Mr. HAHN. Well, he who gives the most equipment gets, obviously—I mean the philosophy is, he who can give the most gets.

You know, it is the Godfather theory. They make them a deal they cannot refuse. Free is still best.

Senator INOUYE. That is very profound.

Mr. Griggs.

STATEMENT OF ALFRED GRIGGS, COCA-COLA OF NORTHHAMPTON, VICE CHAIRMAN, NATIONAL SOFT DRINK ASSOCIATION, ACCOMPANIED BY EUGENE MEIGHER, COUNSEL

Mr. GRIGGS. Mr. Chairman, My name is Al Griggs. I am an independent third generation soft drink bottler from Northhampton, Massachusetts. And I am appearing before the subcommittee this afternoon in my capacity as Vice Chairman of the National Soft Drink Association.

NSDA is the national trade organization of the United States soft drink industry. Approximately 71 percent of the 1,177 soft drink manufacturers are active members of this association.

In addition, the vast majority of soft drink licensors who manufacture the concentrates and or syrups from which soft drinks are

made belong to NSDA. Our members account for more than 92 percent of the soft drinks produced annually in the United States.

I am accompanied by Mr. Eugene Meigher of Arent, Fox, Kintner, Plotkin & Kahn, who serves as anti-trust counsel to the Association. We appreciate this opportunity to appear today in order to provide the subcommittee with NSDA's comments regarding S. 2347.

Our testimony consists of two parts. I will give a brief summary of how the post-mix dispensing business operates in the soft drink industry, and the second part of our statement will be presented by Mr. Meigher, who will detail our specific objections to S. 2347.

In the early 1960s, the practice of lending dispensing equipment to retailers to enhance post-mix volume began. From the mid-1960s to the early 1980s, competition in the post-mix business increased dramatically, and loaned equipment or comparable marketing programs became commonplace throughout the industry.

By 1970, with the expansion of national food service chains, retailers either were provided with loaned equipment and merchandising materials, which are menu boards, clocks and advertising material of that nature, or were reimbursed a fixed dollar amount per gallon for annual gallons sold.

The former choice was typically preferred by independents and local chains with limited capital, and the latter by national chains who would use the funds to purchase equipment and merchandising materials. Consequently, most national food service outlets own their own equipment.

In the early to mid-1980s, competition intensified in the local markets, which are independent local chains, which represent the largest number of post-mix outlets, but generally are characterized by lower syrup volume per outlet.

The advancements in dispenser technology, such as larger capacity, increased refrigeration and more rapid rate of flow have translated to much higher equipment costs, reaching as much as $2,000 per unit, including installation expense.

Due to the financial impact on these outlets of high equipment costs coupled with lower volume, major syrup producers began either to lease dispensing equipment or to provide a bundled program such as equipment service and syrup for an established cost per gallon.

As a Coca-Cola bottler, I am most familiar with that company's program. Beginning in 1988, Coca-Cola USA introduced the total value plan, which offers local market retailers dispensing equipment, service and merchandising materials for a monthly fee, in addition to the price of syrup.

Coca-Cola bottlers may or may not participate in the TVP program. The company estimates that less than five percent of its new equipment placements is loaned equipment. As equipment in loaned equipment accounts requires replacement, the company projects that TVP will generally replace equipment loan programs.

Approximately 50 percent of the post-mix dispensing equipment in the soft drink industry is loaned. The other 50 percent is leased or owned by the retailer. Additionally, 85 percent of all loaned equipment is installed in accounts which buy, according to our estimates, less than 1,500 gallons of syrup per year.

If the soft drink industry is forced to abandon its current equipment programs, smaller retailers, unable to take advantage of such programs, must suffer higher costs and thereby lower returns, or utilize cheaper inferior equipment and suffer loss of quality control.

Post-mix dispensing equipment is often placed on a discounted basis. Retail outlets are given marketing allowances, or sums paid on the basis of syrup purchases, which they can use for a variety of purposes at their discretion, including such things as advertising in local publications, participation in consumer promotions, which require expenditures for point of sale material, and advertising, or equipment purchases.

This is a common longstanding business practice used in a host of consumer and industrial product situations where specialized equipment is needed to merchandize products, or where retailers and suppliers can cooperate on programs aimed at enhancing the value of products to consumers. It is a cost-efficient direct approach for which there is no real substitute.

Subsidizing purchases of equipment which serves a finished beverage product to the consumer is a prudent business policy for beverage suppliers. From my viewpoint, the dispenser in a retail outlet is nothing more than a small bottling plant.

Mr. Chairman, the post-mix dispensing business practices that I have described are the results of intense competition among members of the soft drink industry. Those practices have resulted in providing the consumers of soft drink products the highest quality at the lowest cost in a multitude of outlets.

For the Congress to mandate changes in that competitive climate would be imprudent and unnecessary government policy, imposing additional costs on retailers, many of whom are small businesses, and consumers who are the ultimate beneficiaries of these practices.

Mr. Chairman, as an officer of the National Soft Drink Association, I can tell you that bottlers are divided as to whether the programs that I have described are beneficial to them.

But the issue is whether the market is better served by intrusive Federal regulation or by the free play of competition.

Mr. Chairman, Mr. Meigher will now present specific comments on S. 2347.

Senator INOUYE. Before Mr. Meigher, may I ask you some questions?

Mr. GRIGGS. Yes, sir.

Senator INOUYE. Do you believe that the practice that Mr. Hahn described at the Smithsonian, assuming that his testimony is correct, is proper?

Mr. GRIGGS. Well, my view of competition, Mr. Chairman, is that I will compete as a Coca-Cola bottler in my market in a variety of ways.

Certainly price is one way, marketing support services is another, technological advanced equipment is a third. I am in business to make money, and I do not give away anything. If I choose to bundle the equipment that was described by Mr. Hahn at a particular location for competitive reasons, it might appear as he was describing it that it is for nothing.

My point is that that is just an element of competition which, when I looked at my P&L monthly and yearly, has got to generate profit.

Senator INOUYE. Now, when you provide equipment to a small retailer, at $1 a month as has been testified here, would you permit that equipment to be used to dispense other than Coca-Cola?

Mr. GRIGGS. Absolutely. I am a Dr Pepper bottler, in addition to being a Coca-Cola bottler. And my objective is to form a partnership with that small retailer.

And one of the mechanisms of establishing that partnership is to assist him by placing equipment in his location. I represent Dr Pepper, Canada Dry, Sunkist, A&W, a variety of products. And it is frankly his decision what he wants to have through that dispenser.

Senator INOUYE. Does that equipment say Coke?

Mr. GRIGGS. Yes, sir. And I might add that——

Senator INOUYE. Then I cannot dispense Pepsi-Cola?

Mr. GRIGGS. No, sir. That is correct. I might add in my market I am proud to say that he would most likely prefer Coca-Cola.

Senator INOUYE. Mr. Meigher?

Mr. MEIGHER. Thank you. I will very briefly summarize my written testimony.

Senator INOUYE. Thank you.

Mr. MEIGHER. There are basically three reasons why NSDA opposes S. 2347.

The first is that the legislation is unnecessary. The practices that the legislation appear to be concerned with are below-cost pricing, conceivably price discrimination, practices that have exclusionary or exclusive effects.

All of these kinds of practices are already very well deal with by the anti-trust laws, and these practices over 50 or 60 years have been frequently litigated in anti-trust cases.

There has been no showing that there is any inadequacy in the anti-trust laws, and as a result there is really no showing that there is any need for a change.

Perhaps more important, our second reason is that we believe that the legislation is very likely to reduce competition.

When you look at the basic anti-trust laws, you find a common denominator, and the common denominator is a focus upon the effects of practices upon competition.

The Sherman Act, for example, forbids agreements and unreasonable restraint of trade. The Clayton Act goes after practices that substantially lessen competition in a marketplace. The same with the FTC Act.

All of these statutes have somewhat different standards, but they all come down to the same thing, a focus upon the competitive process.

Now, perhaps that incidentally protects certain competitors, but that is not the primary objective of the anti-trust laws. It is to protect competition.

When you look at this bill you find a very different focus. It is a bill that says nothing at all about protecting the competitive process. It is very clearly a bill that has been designed to protect individual competitive suppliers.

As a matter of fact, when the bill talks about effects, it consistently talks about effects in terms of an effect upon a single competing supplier. And beyond that, it not only deals with the situation where a given supplier might be injured, but it talks about the possibility of a violation when a given supplier might lose a single transaction.

So it is a very protectionistic statute, which certainly does not fit very well in the family of anti-trust statutes. And because it does have this focus upon the loss of an account, it potentially has an effect of deterring those competitors in the marketplace who want to be aggressive, who want to increase market share, who want to reduce prices and pass along the benefits of their efficiencies.

The practices that are the focus of this statute have been litigated about for many years. And almost invariably, when they have been litigated over, they have been found to be reasonable, and indeed in many cases very pro-competitive.

One of the earliest cases—I will not go into the facts of it or the details of it—is an old 1921 case that the FTC brought against Sinclair Oil Company, when it was giving away tanks, underground tanks and pumps to those retailers who were willing to limit their purchases to Sinclair.

The Commission found a violation. The Supreme Court held that the test was: what is the effect upon competition? Let us look at competition. And when it did, it found that basically this conferred benefits on that retailer, who probably otherwise could not get into business because he could not afford the tanks, he could not afford the pumps.

Same kind of practice came up in a series of cases in the 1960s when the FTC looked at similar practices in the ice cream and frozen dairy products industry. In a series of seven or eight cases that were all decided at the same time, involving almost identical practices, the Commission after looking at the matter for three or four years, and looking at it very, very extensively, decided that the effect of the practices was to benefit retailers and in turn to benefit the consumers who traded with those retailers.

As recently as four years ago the Fifth Circuit looked at a case in this industry. It is called Bayou Bottling Company versus Dr Pepper. At that point Dr Pepper and one of its franchisees were on the receiving end of a challenge that practices very similar to this were anti-competitive.

Basically what was going on was that the local bottler for Dr Pepper would go to a retailer, offer him a cooler free, on the condition that if he used the cooler he would put the various products that that particular bottler was offering into the cooler and no others. There were no restrictions on whether other coolers might be put in the store or anything else, but that was what was being tested.

The Fifth Circuit found that that practice was beneficial, and that the relevant question, in the case of the small retailer, is what are the odds that the retailer would have made the investment if he were to bear the direct costs? And that practice was found not to be a violation.

That long practice, or that long history of litigation, I think, has a lot of wisdom in it. It tells us to be very careful about suppressing

or deterring these practices which have been very much tested for more than 50 years, and which have been found to be pro-competitive, not anti-competitive.

Finally, the third reason why we oppose this legislation concerns the lack of clarity in the standard. I mentioned the fact that the effects references are all cast in terms of effects upon individual competitors, not upon the competitive process. That is a major problem.

In addition to that, just to give you a couple of examples, there is a provision that says, leasing at below "fair market value." Fair market value is nowhere defined in this.

It obviously means something different than that which is already very well established in the case law—below cost pricing, something we, at least anti-trust lawyers know something about.

It sounds like a standard which says to the bottler, be very careful not to get too far out in front in your competition, and in fact it may be an invitation to go slower, to engage in me-too pricing, and not to be an aggressive competitor.

The same with the provision that says that he may not extend credit, that is not "usual and customary" in the market. That is an invitation, I take it, to look around the market and to ask what are your competitors doing by way of extending credit? Do not go beyond those people or you are in big trouble.

Well, historically, the extension of credit to customers has been viewed as a pro-competitive move, or initiative, and if two or three competitors were to get together and agree that they were not going to extend more than three or six months credit, they would be indicted if they were discovered. This bill, or this provision, has the same effect as that conspiracy would have.

In short, and for all of these reasons, we oppose this bill.

[The statement follows:]

STATEMENT OF EUGENE J. MEIGHER ON BEHALF OF NATIONAL SOFT DRINK ASSOCIATION

My name is Eugene Meigher. I am a partner in the law firm of Arent, Fox, Kintner, Plotkin & Kahn. My firm serves as antitrust counsel to the association and I appear before the subcommittee today in that capacity. I appreciate this opportunity to present the subcommittee with NSDA's specific comments on S. 2347, which would amend Section 5 of the Federal Trade Commission Act.

NSDA is strongly opposed to S. 2347. There are at least three reasons why S. 2347 should *not* become law. *First,* it is unnecessary. Existing antitrust laws are fully adequate to halt any equipment leasing practice that impairs competition. *Second,* S. 2347 would be harmful. It would *reduce* competition, not increase it. The courts have consistently and repeatedly ruled for the last *sixty years* that equipment loan programs like the ones that S. 2347 would prohbit are beneficial and *pro*-competitive, not *anti*-competitive. *Third,* S. 2347 is unclear. It is confusing and ambiguous, and it would prohibit much more than free fountain equipment, which is its purported focus. Indeed, any form of marketing support from soft drink manufacturers to soft drink retailers would be prohibited.

1. S. 2347 IS UNNECESSARY

Implicit in the proposal to adopt S. 2347 is the view that existing antitrust laws are somehow inadequate to deal with any anticompetitive situations that may arise in connection with the distribution of post-mix soft drink dispensing equipment. On the contrary, existing antitrust laws are fully adequate to deal with any practices in the marketing of post-mix syrup that would impair competition.

The core concern of S. 2347 seems to be that loaning or leasing soft drink equipment at less than "fair market value"—however that should be measured—is harm-

ful. But if loaning or leasing below cost is *harmful to competition*, it is already illegal, both under the Robinson-Patman Act and under the Sherman Act. *Power Replacements Corp.* v. *Air Preheater Co., Inc.*, 356 F. Supp. 872, 889, 897 (E.D. Pa. 1973).

Similarly, if the concern is the use of free or low-cost equipment to restrict competition in the sale of soft drink syrup, that practice can be attacked under either Section 3 of the Clayton Act or Section 1 of the Sherman Act, *whenever it harms competition*. E.g., *Perryton Wholesale, Inc.* v. *Pioneer Distributing Co.*, 353 F.2d 618 (10th Cir. 1965), *cert. denied*, 383 U.S. 945 (1966).

Second, if "giving away" fountain equipment might conceivably result in a monopoly, which is truly fanciful, then Section 2 of the Sherman Act is available. Any practice that is "predatory"—that is, it restricts competition without justification—is illegal under Section 2 if it could lead to or preserve a monopoly. *Janich Bros. Inc.* v. *American Distilling Co.*, 570 F.2d 848, 855 (9th Cir. 1977) *cert. denied*, 493 U.S. 829 (1978).

Third, any unfair method of competition is prohibited by Section 5 of the FTC Act and by the numerous "Baby FTC Acts" in the states.

Finally, there are a variety of state and common law remedies that deal generally with unfair competition and unfair business practices.

For all of the foregoing reasons, we believe that existing antitrust laws are adequate to deal with anticompetitive conduct that might arise in connection with the marketing of post-mix syrup and equipment. No need has been established for the passage of special legislation. Certainly no need has been established to pass legislation that is repugnant to basic antitrust principles.

2. S. 2347 WOULD HARM COMPETITION

S. 2347 departs from traditional antitrust standards in a very substantial way. The basic test applied by all the principal antitrust statutes is whether a practice harms competition. Section 1 of the Sherman Act prohibits agreements in unreasonable restraint of trade. The substantive provisions of the Clayton Act forbid various practices that "substantially lessen competition." Section 5 of the Federal Trade Commission Act broadly declares unlawful unfair methods of competition in or affecting commerce.

In contrast, S. 2347 focuses not on effect on competition, but on effects on a single competitor. In fact, S. 2347 may be violated without any injury at all to competition. A violation is possible even if no competitor is significantly injured. The "injury" aspect of the bill is satisfied if any competitor is "hindered" from selling syrup to a single retailer. This test is not only different than that incorporated in the Sherman and FTC Acts, but also antagonistic to the spirit of those Acts.

A long line of court decisions, stretching back over sixty years, has held that the loan of equipment for use with an associated product is perfectly reasonable and procompetitive. In 1923, the Supreme Court upheld the practice of gasoline refiners leasing gasoline pumps at nominal rates to retailers provided that the pumps be used with the refiners' gasolines. *FTC* v. *Sinclair Ref. Co.*, 261 U.S. 463 (1921). In 1962 the FTC found nothing improper in ice cream manufacturers loaning freezer cabinets to food stores for use only with the manufacturers' ice creams. *Carnation Co.*, 60 F.T.C. 1274 (1962). In 1965 the Tenth Circuit Court of Appeals rejected antitrust attacks on a grocery wholesaler who loaned display racks to retail grocers, but required the grocers to use the wholesaler's goods on those racks. *Perryton Wholesale, Inc.*, v. *Pioneer Distributing Co.*, 353 F.2d 618 (10th Cir. 1965), *cert. denied*, 383 U.S. 945 (1966).

The courts have twice upheld loaned equipment programs in the soft drink industry. *Sulmeyer* v. *Coca-Cola Co.*, 515 F.2d 835, 847 (5th Cir. 1975), *cert. denied*, 424 U.S. 934 (1976); *Bayou Bottling Co.* v. *Dr Pepper Co.*, 725 F.2d 300, 304 (5th Cir. 1984), *cert. denied*, 469 U.S. 833 (1984). In the *Bayou Bottling* case, the court stated that providing free coolers and free service to retailers was "not barred by the antitrust laws. [These practices] are competitive acts."

None of these decisions can be attacked as aberrational or a product of the new "Chicago School" of learning, which some have criticized as overly permissive. Instead, these decisions are consistent, long established, bedrock antitrust law. Thirty years ago, Professor Donald Turner, one of the leading mainstream antitrust commentators, wrote that the lease of a promotional product or collateral service at low or no cost along with another product was not an illegal practice but was merely a form of non-price competition. Turner, *The Validity of Tying Arrangements Under the Antitrust Laws*, 72 Harv. L. Rev. 50, 65 (1958).

There is no basis for reversing course now.

3. S. 2347 IS UNCLEAR

S. 2347 contains a number of expressions that are not defined and that may create unfortunate results in the enforcement of the bill. I will mention just a few examples. The expression, "substantially to restrain or prevent transactions," in subpart (a)(2), is nowhere defined, but it arguably applies even to the situation where a retailer has extracted such a good deal from one supplier that the retailer wants to deal exclusively with that supplier.

Similarly, the bill comes into play whenever there is an effect "to prevent, deter, hinder or restrict other persons from selling * * * to such retailer." However, none of those terms are defined. If there is no exclusionary agreement between the retailer and its suppliers, does the unwillingness of the retailer to deal with a competing supplier "hinder" that supplier within the meaning of this bill? Or if the retailer wanted no more than one piece of dispensing equipment, would that "hinder" the other person's sales? It is not uncommon for retailers to choose to have only one brand of dispensing equipment in their outlets. One does not have to fall back on concepts of conspiracy or monopolization to understand why retailers might make such a choice. If such a retailer's decision "hinders" a potential supplier, then the actual supplier—simply by furnishing any of the services described in (b)—puts itself in peril of a violation. And the violation may be found without any finding of a lessening of competition.

Subsection (b) describes certain practices as "means of inducement," which are components of the violation created by the bill. Such practices, however, have often been reviewed by the courts, and that judicial experience does not support the presumptions created by S. 2347 against the practices. On the contrary, the offer of free goods and services is frequently a form of competitive rivalry. Competition would not necessarily be strengthened by mandating that it take only one form—price competition. Just as public policy does not favor suppressing such forms of competition in other industries, there is no basis for suppressing such competitive initiatives in the soft drink industry.

Subpart (b) is replete with ambiguous language whose most likely effect will be to dampen competition in the market. The phrase "below fair market value" is hopelessly ambiguous and nowhere defined. The bill does not make it clear whether the "market," referred to, is a local market, a regional market or a national market. Moreover, the concept of "fair market value" implies "me-too" pricing, since it evidently departs from antitrust concepts like below-cost pricing. Similarly, encouraging a limitation of credit to a period that is "usual and customary" is an invitation for competitors to go along with the least competitive suppliers in the market. The likely effect of S. 2347 is to eliminate the offer of credit terms as an element of competition. If competitors were to agree to refrain from offering credit beyond a certain term, they would be indicted. The bill achieves the same effect.

S. 2347 would also bar soft drink companies from providing signs, money, or services of any kind to retailers. Thus, all cooperative advertising and all joint promotions and marketing efforts involving soft drinks would be effectively prohibited.

For all of these reasons, NSDA urges that S. 2347 be defeated.

Senator INOUYE. Thank you very much, Mr. Meigher. Then according to your argument, the Alcohol Administration Act is unconstitutional, because that act, among other things, states that the alcoholic beverage industry may not offer inducements if such inducements are free dispensing equipment, and that inducement also excludes the dispensing of other brands?

Or what it says here is that Coors beer may not give you a free dispensing outfit, and say that part of the deal is you do not serve any other beer. Now, in this case, Coca-Cola provides free equipment or $1 a month—part of the agreement is that you do not serve Pepsi-Cola. Would that be a violation?

Mr. MEIGHER. Well, just to take the last question first, there can be a violation if when you look behind the facts you determine that there is below-cost pricing. The Sherman Act would certainly deal with that. And if the facts are that a competing supplier is engaged in below-cost pricing that would be a violation.

Or similarly if you discovered when you looked at the facts that there is a pattern of pricing that is discriminatory, let us say geographic price discrimination, that could be a violation as well.

But to touch upon your first question about the Constitutional aspects of this, I do think we have to remember that the alcohol beverages industry has always been in a somewhat special state.

There is a Constitutional amendment that deals with that industry. The states have powers of regulation of that industry that to some extent displace the anti-trust laws.

But apart from those circumstances, where there has been a perception that the policy of competition ought to be displaced in part or in whole, the basic policy is to support free and open competition, and that is what we are for.

Senator INOUYE. Senator Kasten, do you have any questions?

OPENING STATEMENT BY SENATOR KASTEN

Senator KASTEN. Mr. Chairman, thank you. At this time I have no questions of this witness, but I do have a brief opening statement. I congratulate you on presenting the problems faced by some soft drink equipment manufacturers, those who lease this equipment and some of the smaller syrup manufacturers.

And I understand it, we are going to hear testimony with regard to the competition in the industry. I look forward to the testimony. I know the Judiciary Committee has been granted joint referral, and believe this issue should be looked at by that Committee as well.

My greatest concern regarding this bill is the necessity for an antitrust prohibition which is directed at just one industry. With the general laws that we have to foster competition, the Sherman, the Clayton, and the FTC acts. I think we want to look at whether or not we might already have the framework within which this issue can be resolved. Further, under the Sherman and the Clayton acts, I believe that there are private rights of action with treble damages. I hope to hear testimony on my concern from some of the proponents of this bill.

I apologize to the witnesses for the testimony that I have missed, and I will review their testimony as to their experience in this regard. Whenever we hear complaints from small business people, such as are testifying today, it is important that we investigate their concerns. And I want to work with you in investigating these concerns. Thank you, Mr. Chairman.

Senator INOUYE. Thank you very much. That is essentially the purpose of this hearing, obviously.

We will not get anywhere beyond the hearings, in two weeks or less than that the Congress hopes to adjourn. And legislation of this nature, of this complexity and controversy, will not get through both houses in less than two weeks.

But we are hoping that by initiating these hearings it would begin the necessary dialogue nationally, and this matter will be brought to the attention of Members, not just of this Committee but also of Judiciary. And if we find that facts justify proceeding further next year, that will be done.

So I would suggest that if you do have concerns, you discuss this matter with Members of your delegation, whatever state you are from, and that may have an effect upon whether this Congress will further consider this measure.

We will be receiving all of your testimony, and I will keep the record open for at least two weeks to make certain that all of you will have an opportunity to submit supplemental testimony, if that is your wish, or to make corrections in your testimony.

But to those who are for or against this, do not expect any action on the floor. That will not happen. Something may happen next year, but not this year.

May I now call on Mr. Watkins?

STATEMENT OF JAMES W. WATKINS, VICE PRESIDENT, DR PEPPER CO., ACCOMPANIED BY PHILIP BART, COUNSEL

Mr. WATKINS. Thank you, Senator. First, I want you to know that we sincerely appreciate your, and the Committee's, interest on behalf of consumers in our—and by "our" I mean the soft drink industry.

I am represented today also by our counsel, Mr. Philip Bart of the firm of Morrison & Forester. I am here as an employee and representative of the Dr Pepper Company. But also, because of our association with The 7 Up Company, I am testifying on their behalf as well.

Dr Pepper and 7 Up are the manufacturers of soft drink concentrates as well as finished fountain syrups that are sold to food service operators. By food service operators I mean the McDonalds, the 7-Eleven's of this world. What they then do is mix it with carbonated water to form a finished soft drink that is sold to the consumer.

I would also like to say that both of our companies are members of the National Soft Drink Association, and felt it necessary that we make certain points.

The practice of providing soft drink dispensing equipment either free of charge to food service operators, or more commonly at some form of reduced lease rate or other consideration, is clearly increasing.

We believe that this has a direct negative impact on the bulk soft drink category. By bulk soft drink, I refer to the fact that our industry is really split into two forms of soft drinks: The bottles and cans that are purchased in grocery stores and convenience stores, and the bulk soft drink syrup that predominantly is contained in the silver five-gallon transfer tanks that you see in restaurants.

Food service operators are being coerced into choosing specific brands, whether it be Coca-Cola, Pepsi-Cola, or 7 Up or Dr Pepper, of fountain soft drinks, based upon soft drink dispensing equipment issues, menu board issues, or other items, as opposed to making their soft drink brand decisions solely on the benefits inherent within those brands. More precisely, actual consumer preference.

It is common practice for at least one major fountain soft drink supplier to contractually limit the dispensing of competitive products, brands other than their own. And here I want to quote the actual standard contract of one of these major suppliers.

"One valve," and by valve they are talking about the four or five spigots on that machine you see in a restaurant, "if the equipment has four or more valves, may be used at the lessee's option for dispensing a non-cola non-company post-mix product, but not in any case a product of, and they list a specific competitor, or an affiliate," and again they list that specific competitor.

We have also run into a number of other competitive situations where a major fountain soft drink supplier has provided financially lucrative packages to food service operators, which will include post-mix dispensing equipment considerations.

These are then based on product exclusivity. Only their products, or in the case of the contract previously mentionad, no more than one competitive product. There are over 100 brands of soft drinks in this country, and they are allowing only one.

This is of course of great concern to our companies and our bottlers around the country, and we believe it has a direct and negative impact on our companies as well as our bottlers.

Not only does this greatly influence the food service operator's selection of soft drink brands, but at the same time it prevents the consumer from being able to select the brand that they actually prefer.

We believe that the practice of providing soft drink dispensing equipment free of charge, or at a reduced lease rate, is certainly an unhealthy practice in our soft drink industry, but also is ultimately to the consumer.

[The following information was subsequently received for the record:]

QUESTIONS OF SENATOR GORE AND THE ANSWERS THERETO

Question.

1. **Does Dr Pepper or Seven-Up ever provide equipment for free or at low cost to their bottlers, wholesalers, or customers? If so, please describe any program or situation in which either company has provided equipment to those customers.**

ANSWER:

Both Dr Pepper and Seven-Up individually have programs to assist their bottlers in the purchase of Dr Pepper and/or 7Up identified post mix dispensing equipment. However, the purpose of this program is to provide a merchandising/advertising medium for our brands, as opposed to necessarily assisting bottlers in the purchase of equipment only. The Dr Pepper Company also makes this program available to direct buying syrup customers, but again, this is a merchandising/advertising effort as opposed to providing free equipment. Instead of providing the equipment to our bottlers or customers, we may provide them a small quantity of product free of charge to help defray the cost of customizing this equipment with any of our brand logos.

Question

2. **Are Dr Pepper or Seven-Up products ever dispensed in equipment provided free or at low cost by Coke or Pepsi? If so, does Dr Pepper or Seven-Up contribute to the cost of buying, installing, or servicing such equipment?**

ANSWER:

There are accounts that do dispense Dr Pepper or Seven-Up products on equipment owned by our competitors. In many cases Dr Pepper or Seven-Up is then asked to contribute its "fair share" of the installation and/or ongoing service cost.

Question

3. **Does Dr Pepper or Seven-Up allow its bottlers, wholesalers, or customers to handle competing flavors such as Sprite or Slice without restrictions? If not, please explain any restrictions that are imposed and why they are necessary.**

ANSWER:

In the bulk soft drink market, Dr Pepper and Seven-Up both allow their bottlers, wholesalers, and customers to handle competing flavors such as Sprite or Slice without restrictions. Some of our franchise bottlers also act as Sprite or Slice distributors and in many cases actually distribute a greater volume of the competitive product than they do of our brand.

Question

4. **"Does Dr Pepper or Seven-Up engage in research and development of fountain equipment? Please describe any of the company's activities in this area."**

ANSWER:

Dr Pepper and Seven-Up work closely with most major manufacturers of fountain soft drink dispensing equipment to ensure that the equipment being developed and put in the market place is of sufficient quality and capability to produce the highest possible finished soft drink. We have ongoing policies which require that, prior to any of our brands being served in any piece of fountain equipment, our research and quality control labs must have thoroughly tested that equipment, and we work closely with such manufacturers on any possible modifications or improvements.

Senator INOUYE. Thank you very much, Mr. Watkins. If your company rules permit, could you share with us a copy of the contract that you just quoted from?

Mr. WATKINS. I do not have a specific copy with me, but we could share it with you. Of course.

Senator INOUYE. We would just like to have it for the files.[1] Do any of you have contract forms like that that you would like to share with this Committee?

Mr. WATKINS. Senator, I am referring to what is a generic contract and they would simply fill in the blanks for a variety of customers. We would like to provide you with a blank copy of that contract.

Senator INOUYE. Senator Kasten?

Senator KASTEN. I mentioned in my statement the Sherman Act, the Clayton Act, FTC Act, all which are geared toward fostering competition. And, I understand that the basic problem that you are describing here. With the laws that are on the books, have you ever worked with an attorney or pursued a case? Or have others pursued cases in this area and been unsuccessful? Or have you not pursued the legal course?

Mr. WATKINS. To answer your questions, sir, I cannot specifically discuss the legal practices of other companies. Our purpose in being here today is to comment on what we feel is an unfair practice in our industry, not necessarily to state that this bill as it is proposed is an end-all or a better solution.

But clearly there is an anti-competitive issue involved. I do not know the specific answer to your question.

Senator KASTEN. You do not know then if you or others have tried the FTC, Clayton, or Sherman Acts?

Mr. WATKINS. Not to my specific knowledge.

Senator KASTEN. Can any of you help me? Mr. Hahn?

Mr. HAHN. I have an unusual position in this hearing in that I am probably the only original equipment manufacturer testifying. And I am dictated to by Robinson-Patman.

As an original equipment manufacturer, Robinson-Patman dictates how I have to, or should conduct my business relative to competitive practices and price structure, essentially.

In my position, where I am eliminated from the marketplace, is by the two syrup companies, one or either or both or however the deal goes, where they come in after my equipment has been specified, and in many cases purchased for the project, that purchase order is cancelled. And I then have the cost of everything involved and have to eat it. I have no recourse.

And it is cancelled because one of the representatives of the major syrup companies came in and offered him a deal that he could not refuse. And I call that the Godfather theory, because he sits there with the power of, you can have it free, and I am sitting there—I mean, I am eliminated. I cannot compete on that level.

I cannot give him what I make because the essence of our business is in what we manufacture, sell and install.

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[1] The contract is in the Committee files.

Senator KASTEN. We are already trying to deal with unfair competition through the general antitrust laws. I do not know all the details of all these laws, but among these general laws that are already there to foster competition, you feel there is no law that addresses your concerns?

Mr. HAHN. Well, in discussing this generally with attorneys that would be qualified, it is, unless you can get the testimony, unless you can get the testimony of the participants and you have to go through the legal process, which is extremely expensive. It probably costs $50,000 to $100,000 to pursue a case like that.

And while it personally would be worth it to me, I have been asking the people if they would cooperate and testify. They all said no.

Senator KASTEN. Mr. Meigher, did you want to make a brief comment?

Mr. MEIGHER. Yes. Earlier I talked about a case that was decided in the Fifth Circuit just four years ago. It is called *Bayou Bottling Company* v. *Dr Pepper.*

And that case involved in this industry at least the closest instance of these kinds of practices being tested. But there have been several other cases in the industry.

For example, only a few years ago Judge Pollock, in the Southern District of New York, looked at the practice of exclusive dealing that exists between bottlers and franchise companies, and thoroughly analyzed the practice, found it to be lawful. As far as I know, every time that exclusive dealing has been tested within the industry, it has been vindicated.

Now, if this gentleman's concern is something different, for example, if it is the possibility of below-cost pricing, there is Section 2 of the Sherman Act. And if he could establish that there was below-cost pricing he would have a Section 2 case.

I do not want to minimize the difficulty of that kind of case. But it is available, and plaintiffs do succeed in proving those kinds of cases.

Senator KASTEN. Mr. Chairman, thank you.

Senator INOUYE. Thank you very much, gentlemen. Our final panel consists of Mr. Mark A. Imbesi, General Manager, Food Service Division, Imbesi Bottling Group of New Jersey, Mr. Richard Crawford, Director, Federal Affairs, National Restaurant Association of Washington, and Mr. H. Ronald Harris of Marblehead, Massachusetts.

STATEMENT OF MARK A. IMBESI, GENERAL MANAGER, FOOD SERVICE DIVISION, IMBESI BOTTLING GROUP

Mr. IMBESI. Thank you, Mr. Chairman.

I am Mark Imbesi, the General Manager of the Food Service Division and one of the principal owners of the Imbesi Bottling Group, a 7 Up and RC bottling company from the Atlantic coastal states. We have food service operations in the Delaware Valley and the Maryland area.

I am testifying in support of S. 2347. Today I would like to speak to you about the current situation regarding equipment give-aways or, better put, the providing free of charge of dispensing equipment

for the purpose of excluding competition, engaged in by our competitors.

This practice, which started several years ago, is continuing to escalate, despite claims by our competitors that they plan to discontinue the equipment programs and charge for service.

The effects and injury to my business by this practice can be measured in lost business revenues, decreased franchise value, business opportunities lost, and immeasurable lost sampling opportunities for our products. Some examples. One of the major customers lost by my company due to this program was ARA, the largest vending and food service company in the country.

I was told by their vice president of purchasing that he liked 7 Up, would like to continue using 7 Up; however, if ARA did stay with 7 Up, they would jeopardize their free equipment programs that had been introduced by our competitors.

This was in 1985. In the previous year of business, my company did over $250,000 worth of business with ARA.

Another customer which was lost specifically due to this program was the former Gino's fast food chain. Gino's, based in Philadelphia, ran over 200 fast food and family style restaurants.

They purchased 7 Up syrups from my operation. Shortly before the chain was sold to the Marriott Corporation, the Coca-Cola Company provided free all new equipment to all locations. The end result was that our competitors became the exclusive soft drink purveyor to the Gino's chain in all locations.

Hyatt Hotels in Baltimore, Maryland, and Cherry Hill, New Jersey, were our accounts that were lost due to our competitors providing free all new equipment. And in these accounts we were providing equipment, but we still lost the account because Hyatt and management of Hyatt did not want to jeopardize their national equipment programs proposed by our competitors.

Pargo's Restaurant and Saloon, a growing chain of restaurants and saloons, whose base of operation is outside of our franchise area, however my company was serving two locations in the Baltimore area. Again, we were providing equipment, but lost the account because Pargo's headquarters decided to go with a national free equipment program.

H.A. Winston, a chain of saloons in the Philadelphia area, purchased 7 Up for over ten years. Our competitors came in with a free equipment program and became the exclusive soft drink supplier.

Other major accounts where we lost business due to these programs were Resorts International Hotel and Casino, several independently owned Holiday Inns, the Delaware Valley Buying Cooperative, a buying cooperative for diners and restaurants in the Delaware Valley, Kentucky Fried Chicken, franchise-owned, that is independent, franchise-owned locations, and corporate-owned Po Folks restaurants, just to name a few.

The list could go on. I have named major and recognizable accounts. However, our competitors, with their free equipment programs, have had an even greater impact on the independent account side of the business.

One of our most often heard comments from independent retailers is "I would love to have 7 Up, but this is not my equipment, "or

"They will not let me use anything else but their products, "or "If I use your products I will be charged rent."

These are lost opportunities. In summation, these programs have cost my companies over $2 million in lost annual revenue and decreased the value of my franchises by limiting the number of units sold, and have diminished the sampling ability of my franchised brands, and have effectively locked out my products out of certain market segments.

I urge you to enact S. 2347. Thank you.

Senator INOUYE. Thank you very much, Mr. Imbesi.

Are you saying that your competitors in providing free dispensing equipment require the beneficiary to use only their products?

Mr. IMBESI. In most cases, only their products, but they specifically target against my product, 7 Up. In other words they say, if you are going to have a five-head or six-head or four-head dispenser, you can have one valve open, but the one brand you must carry from us is our imitation of 7 Up.

Senator INOUYE. Do you mean there is a written contract to that effect?

Mr. IMBESI. We see this very, very frequently written into contracts in longhand. It is not necessarily typed in.

As Jim Watkins had pointed out, they have blank spaces where they can fill in, depending on the brands they are marketing against.

Senator INOUYE. And if they do violate that provision, the equipment is taken away?

Mr. IMBESI. It is sometimes taken away. We often challenge these customers to call their bluff. It is sometimes taken away. Most often, they are charged a rental fee which they had not been paying, which really puts us at a great disadvantage.

They say, if I do not use your products—your products are very competitively priced, but if I do not use your products I am going to be charged a rental fee, which can amount to several hundred dollars a year. The customers say, we like your products, but I do not know that I want to spend that much extra when I could get it for free.

Senator INOUYE. In a food dispensing shop or restaurant that has this free equipment, can that restaurant serve bottled 7 Up?

Mr. IMBESI. It can. Of course they can do anything they choose. However, logistically it becomes very, very impractical, because the waitresses or the waiters or the servers of the restaurant, instead of going and taking a glass and getting all their soft drinks in one location, which is commonly done now, they would have to move onward to another location within the restaurant.

The second problem would be economically. Post-mix dispensed beverages, fountain syrups, are much more economic, have a greater economic benefit to the restaurateur, to the merchant, than do bottled products.

Senator INOUYE. Thank you very much, Mr. Imbesi.

[The following information was subsequently recevied for the record:]

QUESTIONS OF SENATOR GORE AND THE ANSWERS THERETO

Question 1. I understand that your business includes the rental of fountain equipment as well as the sale of fountain syrup. Do your rental agreements with your customers require the purchase of any of your syrup? Do they relate in any way to the sale of syrup?

Answer. Senator, I understand the first part of your question and yes, some of our agreements require the purchase of our syrup. That is because we sometimes lease equipment and the rental due is the purchase of a minimal amount of syrup in dollar form for the year.

I am not sure what you mean in the second part of your question. If it means, do we restrict the selection of brands that our customers can sell, the answer would be no.

Question 2. What is the normal term of your rental agreements with your customers for fountain equipment?

Answer. Generally, five (5) years.

Question 3. Can the rental agreements between you and your equipment customers be terminated at will by either party or is there a contractual agreement for a particular time period?

Answer. There is a contractual period for five (5) years provided both parties fulfill the terms of the contract. Such as, we are required to provide service in a reasonable, timely and businesslike manner and the customer is required to pay their bills in a reasonable, timely and businesslike manner.

Question 4. Based on your experience, when the syrup companies loan equipment for free or at a reduced price do they always require the recipient to buy a certain kind of syrup? When purchases of syrup are required, must the purchases be made directly from the syrup company, or can the recipient of the equipment buy syrup from an independent wholesaler?

Answer. It is my experience that when the syrup companies loan equipment free or at a reduced price, there are always certain brands that are specified. Those brands need not necessarily always be purchased directly from the syrup company. They may be purchased directly from an independent wholesaler who purchased those brands from a syrup company. So, in essence, the customer who received this equipment package can only deal with the products which are originally manufactured by the syrup companies.

Question 5. Are you aware of any independent syrup wholesalers that loan equipment for free or at a reduce price?

Answer. I am not aware of any independent wholesalers who independently loan syrup equipment for free. However, many wholesalers contract with individual accounts at less than their published pricing. This is generally to reflect some savings that the wholesaler has incurred and wishes to pass on to his customer.

Question 6. If S. 2347 is passed, will that result in higher overall costs for fountain beverages to retailers, particularly restaurants and taverns? If so, are those increased costs likely to be passed on to the retailers' customers?

Answer. It is likely, especially to restaurants and taverns that their overall costs for fountain beverages will be increased, however slightly. Those very minimal increased costs are not likely to be passed on retailers' customers because that increase is so minuscule. Allow me to give an example: Your average tavern/restaurant owner purchases between 3.5 and 4 gallons of syrup a week. He generally has two (2) dispensing stations/guns. The service charge on those guns is somewhere in the $10–$14 range. For argument's sake, we'll use $14.00. the price he pays for syrup per gallon is somewhere between $5.50 and $7.00. Again, for argument's sake, we'll take the higher cost. One gallon of syrup makes one hundred twenty eight (128) six ounce (6 oz.) drinks. A restaurant/bar owner generally sells soft drinks for no less than $.50 per drink.

4 gals. times 128 x $.50	$256.00
less 4 gals. times 7	−28.00
less weekly service	−14.00
Total net profit on drink sales	214.00

This equals an 84% profit.

You could look at the service charge for equipment as a cost per drink. In this case, 512 drinks divided into $14 is equal to $.03 per drink. It is hard to imagine how these costs could or should be passed on to the retailers' consumers.

It should also be noted that by charging for the equipment will enable syrup wholesalers to maintain low syrup pricing.

Question 7. Do any of your customers who rent fountain equipment from you or own their own equipment offer both Coke and Pepsi, or more than one brand of any flavor of soda? If so, what percentage of your customers do that?

Answer. Approximately two-thirds of the customers who rent fountain equipment from us or own their own equipment offer either Coke or Pepsi. All of our customers who we provide equipment to offer more than one brand or one franchised companies' brand or brands.

Question 8. Do both Coke and Pepsi invest in research and development of fountain equipment? If so, in your judgment is that an element of competition between Coke and Pepsi? Could S. 2347 reduce that competition?

Answer. I have no way of knowing what research and development is conducted in fountain equipment by Coke and Pepsi. I do however know that many of the equipment manufacturers conduct their own research and development and use that as a point of competition between the equipment manufacturers. I can only see S. 2347 increasing that competition between equipment manufacturers since more people will be in the business of selling equipment.

Question 9. Have you tried to market your fountain equipment to Coke and Pepsi for their use in their free or reduce price equipment programs? If not, why not? If so, what was the result?

Answer. Senator, we are not a fountain equipment manufacturer. We are a franchisee of the Seven-Up/Dr. Pepper Company, Royal Crown Cola Company, The Click Corporation, The Schweppes/Canada Dry Company and we are also a Coca Cola wholesaler.

Senator INOUYE. Mr. Crawford.

STATEMENT OF RICHARD CRAWFORD, DIRECTOR OF FEDERAL AFFAIRS, NATIONAL RESTAURANT ASSOCIATION

Mr. CRAWFORD. Thank you, Senator. I appreciate the opportunity of appearing before you. You more than most other Senators really have been sympathetic and a champion for the hospitality industry over the years, and so it is a pleasure to appear before you.

One hat that I wear is I am the Director of Federal Affairs for the National Restaurant Association. Another hat I wear is that I am the treasurer of a private club in town, the National Democratic Club. I find it ironic, the chair that I am sitting in belongs to Mr. Quayle. There is a nameplate here.

My testimony will reflect my employer, the National Restaurant Association. But if there are any questions, I might put on the other hat as an officer in a small restaurant operation and private club.

The National Restaurant Association is a trade association of about 14,000 members. In that, we represent over 150,000 food service outlets within the country.

Our Association must respectfully oppose your legislation for several reasons. Most of these have to do with the economic impact it would have on our members, and also for the concern for the quality of the products that we serve to our customers, which we believe would suffer if this legislation were to be enacted.

If your legislation were to pass, we would think that it would deny suppliers an effective means of competing for restaurant business which has existed for many years. Cooperative and promotional subsidies of soda dispensing equipment are common and long-standing practices, not unlike promotional incentives used in other businesses, such as volume discounts and even the familiar baker's dozen.

Prohibiting cooperative subsidies of dispensing equipment will obviously increase a food service operator's capital outlay for equip-

ment. It would be fully obvious that increased operational costs would be paid for by the consumer.

Recently, our data indicates that seven out of ten eating and drinking establishments had gross sales of less than $500,000 annually. Such small operations would be particularly hard hit by the increased cost of equipment procurement and maintenance.

My industry is basically composed of small businesses, and this is reflected in the fact that over 50 percent of all restaurants fail within the first year. You know, it is often said in my industry that you could make a small fortune; the only problem is you have to start out with a rather large one.

The legislation would also likely result in poorer quality fountain drinks. The great bulk of the R&D into the soft drink equipment and technology has come directly from the soft drink companies themselves. If suppliers are not free to provide those improved technologies in the form of subsidized equipment, they will have fewer incentives to invest in continued R&D.

Similarly, food service operators will be less likely to replace outmoded or obsolete equipment and maintenance of equipment is likely to become less predictable. Since the quality of the final delivered drink is intimately associated with the correct match of product, equipment, and maintenance, the likely result is poorer quality fountain drinks for the consuming public.

Again, this impact would be most severe among our smaller operators, who may lack the capital resources to make frequent changes in dispensing equipment and would thus lose their capacity to match other capital-intensive competitors.

S. 2347 unevenly focuses on soft drink fountain equipment and ignores the common application of similar cooperative subsidies in other food supply channels, such as the bottled water dispensers, ovens for point of sale sandwich heating, coffee services, especially the gourmet or espresso varieties, canned soft drinks in vending machines, and chips and snacks found in supermarkets.

Logical extension of this bill would also entail regulation of all commercial promotions and ultimately limit all competition to purchase price alone.

To conclude, we again thank you for the opportunity to present our views on this legislation and the Association asks that you consider not only the economic impacts which would result from your legislation, but also the effect on quality, product quality and consistency for the consuming public.

Senator INOUYE. Thank you very much, Mr. Crawford.

Putting on your hat as manager of this private club——

Mr. CRAWFORD. I am the treasurer of the Democratic Club, sir.

Senator INOUYE. Do you have free dispensing equipment?

Mr. CRAWFORD. No, sir, we own our own equipment.

Senator INOUYE. Now, what is the general practice? Let us say I go into a restaurant that has received free dispensing equipment from Coca-Cola and a customer places an order with the waitress, bourbon and 7 Up. What will she do?

Mr. CRAWFORD. More than likely, the restaurant would have a mix of soft drinks. It might be a bottle or can of 7 Up, as opposed to coming from a post-mix.

Senator INOUYE. You say more than likely. In other words——

Mr. CRAWFORD. I drink my bourbon straight, Senator.

I know in the businesses I have worked in, the restaurants, the bars that I have worked in, a product that has market penetration such as 7 Up would have to be carried because of consumer preference.

A point I think needs to be reiterated, and that was made by Mr. Griggs, I believe, and that is is that the equipment really is not free. Ultimately, someone is going to pay for that equipment. There is no such thing as a free lunch, and it will be paid for by the consuming public.

Senator INOUYE. How?

Mr. CRAWFORD. Well, perhaps Mr. Griggs could come back, but he was talking about bundling together the costs of his business, and part of the cost of his business apparently in his accounting procedure is how much he subsidizes this equipment.

He is going to make that up somehow. I assume the way it would be reflected is that he will be charging more for the syrup or the other goods and services that he provides.

Senator INOUYE. When the competitors have been wiped out.

Mr. CRAWFORD. I tell you, my feelings at this moment are that most of the time the Restaurant Association always feels as though it is being picked on. I think my feelings at the moment probably are analogous to the Reagan Administration, what they thought about the Iran-Iraqi conflict: A pox on both their houses, so long as we benefit.

Unfortunately, the reason that none of us wanted to see that conflict go on, perhaps it was the human, the cost in human suffering.

You look at one of the first witnesses, Mr. Jason over there. He is being squeezed out. No one is actually after him, I suspect. He recognizes that. It is just a fact of the economic competition.

Senator INOUYE. Thank you.

Mr. Harris.

STATEMENT OF RON HARRIS, BETTER BEVERAGES, INC.

Mr. HARRIS. Thank you, Mr. Chairman.

My name is Ron Harris. I own and operate Better Beverages, Incorporated, of Cerritos, California, which is just outside the Los Angeles area. My customers are restaurants, bars, taverns, fast food establishments, clubs, and sometimes schools and military installations.

My father began selling beverage equipment in the late 1950s, and I have continuously been involved in the business for 23 years. I am here today in support of S. 2347, but before I go on I would like to state my admiration for the way you, Senator, handled the Iran-Contra hearings. I thought it was fantastic.

You have already heard the stories of how our industry evolved, and had its beginnings, from my colleagues, and how beverage disposing equipment giveaways started. There are a few areas that have not been discussed that I would like to bring to your attention.

Recently we have seen both Coke and Pepsi try to increase their market shares by buying Dr Pepper and 7 Up. Fortunately for the

consumer, the FTC fought those acquisitions. In its complaint against Coca-Cola, the Commission charged that the acquisition of Dr Pepper would substantially lessen competition in the market by increasing the likelihood of collusion and by making it more difficult for new firms to enter the market and more costly for current firms to compete.

The Commission alleged that these factors would likely lead to increased prices and restricted output of carbonated soft drinks. I question that if it was anti-competitive for those companies to buy out their competitors, how can they be allowed to run the beverage-dispensing equipment industry out of business by placing equipment in restaurants and taverns at little or no cost?

Those of us appearing here today and hundreds of small companies that are unable to attend cannot compete against this type of practice. I have a letter here that I would like to submit in which Pepsi-Cola offered one of my accounts, a Mexican restaurant chain in southern California that I have serviced for many years, $10,000 to convert to Pepsi-Cola.

Senator INOUYE. What does the letter say?

Mr. HARRIS. I quote: "You may use this check in any manner you choose." They did in fact take this account away from my company. Like I say, I will submit the letter and save you the time of reading it.

Senator INOUYE. Without objection, it will be made a part of the record.

Mr. HARRIS. I have another letter from a very small restaurant in the San Fernando Valley that I would like to submit.

This is a handwritten letter by one of my customers.

Senator INOUYE. Same order.

[The letters follow:]

FOOD SERVICE
Buena Park, CA, February 11, 1986.

THE RED ONION,
E. Dominguez Street, Suite H, Carson, CA.

DEAR ——— : Our pricing according to our January 21, 1986, meeting is about $1.15 less than R.C. per 5 gallon tank of Pepsi-Cola. Our lemon lime flavor, Slice, is $6.05 less per 5 gallon tank of 7 Up. 7 Up will replace Slice later in 1986. Based on estimated volume of 12,000 gallons, and an average price savings of $2.75 per 5 gallon tank, we could increase profits by $6,600.00 on syrup.

Bar gun equipment for stores would be on loan from Pepsi by process of waiving allowances.

Also, we will give you a check for $10,000.00 to convert to Pepsi. You may use this check in any matter you choose for The Red Onion.

Service is now operational for nights and weekends. Pepsi will guarantee response times. If a call is received before 9 p.m., we will be there that day. After 9 p.m., we will work with Red Onion to decide what will be a reasonable arrangement.

We will have a marketing manager work with your marketing personnel to develop creative ideas to expand and grow your business.

Finally, based on all factors I have listed above, the total package would be a savings of approximately $17,000.00 this year. In addition, we will develop a market fund for Red Onion to assist in any promotion.

Pepsi-Cola is looking forward to becoming a partner with Red Onion. If you have any questions, please call.

Sincerely,

JON LARSEN,
Key Account Manager, Pepsi-Cola Bottling Group of Los Angeles.

KURT SCHOENHOFF,
District Sales Manager, Pepsi U.S.A.

SCOOPS REST,
Ventura Blvd., Studio City, CA

This letter is being written as a request to release me from my Bar Master lease dated 6/1/84 regarding the soda machines, due to the fact I got a free equipment from Coca Cola and feel it does not make good business sense to pay for something I can get free, and also due to economic reason to save money in this difficult time.

I would like to take this opportunity to thank you all for the good service you always give me.

Thanks again,

____ ____
____ ____

Mr. HARRIS. Today, because of programs like these, Coca-Cola and Pepsi-Cola control approximately 85 percent of the fountain soft drinks being sold. Caught in the middle of the cola wars, of course, are those of us appearing here in this room today, plus hundreds of small businesses that collectively employ thousands of people whose livelihoods depend on their being able to sell and service beverage-dispensing equipment systems.

The immediate impact on the consumer is readily seen by the absence of soft drink brand alternatives in restaurants and bars. Ask yourself, have you ever had a choice between a Coke and a Pepsi in a fast food restaurant?

Beverage-dispensing equipment companies that would normally rent a piece of equipment for approximately $600 a year are not finding customers in the wake of these free equipment giveaways. An average restaurant or bar that requires equipment to dispense beverages would purchase equipment costing $3,000 or would rent it for approximately $750 a year. These sales and rentals are being lost to the free or loaned equipment which has flooded our market.

It is almost impossible to calculate the total financial impact that these giveaway programs have had on the beverage-dispensing equipment industry during the past ten years, but an educated guess would be revenue losses in the hundreds of millions of dollars.

It is estimated that there are 500,000 food service outlets in the United States. If half of them have free or loaned equipment with a fair market value of $3,000, it would mean that there is $750 million worth of beverage dispensing equipment in the market today at little or no charge.

Worse yet, the remaining 250,000 restaurants in the market, will inevitably be targeted for these free equipment programs.

In the last 15 years, the fountain industry has grown by approximately 30 percent. Industry forecasts estimate by the turn of the century more than 40 percent of the soft drinks sold in the United States will be dispensed through fountain equipment. This growth is fueling the Coke and Pepsi appetite to dominate the market.

I would like to take a quick moment and identify a few of my colleagues in this room who have come here today to support S. 2347. Behind me, we call him the father of the industry, Mr. Jack Starman, 82 years old, and working since 1935 in this industry. His son also works in it. He has other relatives that range to his nephews and grandchildren.

Mr. Jason, who spoke earlier, is second generation, as he said. I have the family of Roviaro's from Chicago, there is a brother and sister here. The brother is a twin. There is another sister at home

minding the store. The mother and father work in the industry. A grandson works in the business, an uncle works in the business, and about 20 other employees.

Mr. Bernie Gottlieb from Philadelphia. The Simon family from here in Washington, D.C., have been in business since 1948.

I would like to name them all. They are all dear friends and they are all dear colleagues, and we are fighting for this issue because it is the survival of our business. As we see it, it is a competitive business. We encourage competition. We are ready to fight competition in a fair and open marketplace. But we need an opportunity to fight on an equal scale.

Unless we do something today to stop these unfair competitive practices and giveaways, the direct result will be the end of the beverage-dispensing equipment industry as we know it and, of course, the loss of many thousands of jobs, obviously, to a number of families and their dependents.

I would like to make a statement or two in regards to some of the things I have heard here. Mr. Griggs spoke about a new program in 1988 that Coca-Cola has initiated and this basically confirms, in my opinion, that they (coke) have been loaning equipment at no charge and are now interested in doing something about it and getting money for it. They are replacing equipment that is out there on loan with new equipment but they are going to start charging for it.

I would also like to point out the practice of giving away equipment has been going on for about 20 years, and it has taken us in this industry this long to get to this point of being in a room like this to appeal our case.

The programs that the Coca-Cola Company and/or the Pepsi-Cola Company have initiated through the years have come and gone. Their management teams have come and gone. Their whole philosophies have changed from year to year, or maybe every two or three years. The ladies and gentlemen in this room that are in the independent beverage dispensing industry have been here and have stayed here and have fought to deliver quality beverage products and services to the restaurants Mr. Crawford represents for over 50 years.

We are the innovators of the beverage-dispensing equipment. We are the people who go to the design people like Sandy Hahn of Perfection Equipment Co. and Mr. Mark Chudnow of Chudnow Mfg., who has been making equipment.

Mr. CHUDNOW. Since 1921.

Mr. HARRIS. Thank you, Mark, and thank you for being here. And the companies like his sometimes do not get the chance to sell their equipment because "it's not approved". But yet every specification in his (Chudnow Mfg.) equipment is as good as anybody else's on the marketplace.

We are the people that go to the design houses. We are the people that go to the manufacturers and make the recommendations of things that we see wrong and the improvements that need to be made. We, as an industry, have been responsible for approximately 25 to 30 percent of all the fountain soft drink equipment sold in the country.

As we say, we are getting squeezed. I would also like to—I wish Senator Kasten was still here because he is probably not aware his State, Wisconsin, is the only State where there is a law against giving away free beverage-dispensing equipment in the soft drink industry.

They (Wisconsin) found out in the early 1970s that they needed to put together a law, and I believe it is similar to the laws that prohibit the dairy companies from giving away dairy equipment for exclusive use of either their milks and/or ice creams and so on, similar to the law that you have designed this bill under in relationship to the BATF. (Federal Alcoholic Administration Act, 27 U.S.C. Section 205).

I would also like to address something that the attorney over here spoke to—and I am sorry I did not catch his name. But he brought up an issue regarding the Bayou Bottling and Dr Pepper. He spoke about a free ice cooler arrangement that stimulated business. Maybe so, but basically all restaurants need beverage-dispensing equipment, mainly because it is one of the most profitable parts of the restaurant sales.

Free equipment limits the number of flavors a restaurant may dispense, but, more importantly, at the exclusion of other competitive brands, which I think is anti-competitive.

Mr. Chairman, I thank you and I urge you to approve S. 2347 and have it enacted into law to preserve our small industry and to keep competition alive. Thank you very much.

[The following information was subsequently received for the record:]

BETTER BEVERAGES BAR-MASTER,
October 27, 1988.

Senator ALBERT GORE, Jr.,
Chairman, c/o Consumer Subcommittee of the Committee on Commerce, Science, and Transportation, Room 227, Hart Senate Building, Washington, DC.

DEAR SENATOR GORE: As a proponent of S. 2347, I want to thank you and your staff for helping bring S. 2347 to this point of legislation.

In response to your questions, I have outlined my answers below and following:

Question 1. I understand that your business includes the rental of fountain equipment. Do your rental agreements with your customers limit, or involve in any way, those customers' purchase of fountain syrup?

Answer 1. I am enclosing one of our typical service contracts for your perusal, highlighting those areas under question. You will note our only reference to the use of fountain syrups is defined by using quality products. Our reasoning for this statement is that there are substandard products and products that are not manufactured to be dispensed through beverage dispensing equipment. Should a customer use such products we could not guarantee the performance of the equipment and we would hold the customer responsible for any damage or maintenance which could be caused by such use. Furthermore, it is illegal in the state of California, as it is in many states, to tie a customer to a particular product or product line in conjunction with the rental or lease of a piece of equipment. Unfortunately, these laws do not necessarily cover "loaned or free equipment."

Question 2. What is the normal term of your rental agreements with your customers for fountain equipment?

Answer 2. We have four year terms as a criteria for recovery of our investment and to make a profit. Although most beverage dispensing equipment has a longer life expectancy, we have found that our cost of service and maintenance begins to increase after that period of time. We may also find a need to adjust our term in the near future due to the changes that have become effective from the Tax Reform Act of 1986. The loss of Investment Tax Credits and the changes in the depreciable life of equipment have undoubtedly increased our cost. If we are to remain competitive we will either have to increase our rates or extend the life of our agreement. Compounding these basic problems of competition, of course, are the "free" or loaned at

substantially reduced rates of beverage dispensing equipment being introduced into the market, principally by Coke and Pepsi.

Question 3. Can the rental agreements between you and your equipment customers be terminated at will by either party or is there a contractual agreement for a particular time period?

Answer 3. Our agreement only allows for termination under specific conditions as outlined in Paragraph #9 of our agreement. As a prudent businessman, we have made exceptions for various reasons—but we normally enforce the agreement during its original term, even to the extent of bringing legal action if necessary. We feel we have made a substantial investment, not only in the equipment cost, but also in the hiring of sales and service personnel who receive commissions, salaries, and company benefits to maintain and service the equipment for those customers.

Question 4. Based on your experience, when the syrup companies loan equipment for free or at a reduced price do they always require the recipient to buy a certain kind of syrup? When purchases of syrup are required, must the purchases be made directly from the syrup company, or can the recipient of the equipment buy syrup from an independent wholesaler?

Answer 4. Unequivocally, yes!! With over 20 years of experience in this industry, I have never seen Coke or Pepsi loan equipment without mandating the products that a customer could use in conjunction with receiving free or loaned equipment.

To answer the second part of your question is more complex. If the equipment is free or loaned by a bottler, then that bottler would require the customer to purchase products directly from them. But, if the equipment is supplied by the parent companies of either Coke or Pepsi, then they will normally direct that the customer purchase products from their bottler affiliate, especially with Pepsi because they do not use the type of distribution network that Coca-Cola does. They (Coke and Pepsi) may also negotiate the price the customer will pay for their products and then have an independent wholesaler become a delivery ageny. A delivery agent only gets paid a specific price per gallon of product delivered. Currently, the Coca-Cola delivery agent price is 33¢ per gallon—hardly, if at all, worth the effort for those of us in the syrup business. If you consider the cost of operating your business and the benefits you have to provide in all the regulations and demands that are made on you, 8% (of *our* product cost) is not a lucrative reimbursement. Although Coke does have independent wholesalers to distribute products through, we have seen them acquire over 30% of the bottling network throughout the United States in the last few years, and be instrumental in the purchase arrangements of another 30+% percent, we see more and more of their business being placed with their own bottlers rather than through the independent wholesalers. This causes those of us who are in the syrup distribution business to question if the bottler is receiving some form of special marketing or distribution reimbursement for delivery of these products. It seems highly unlikely that bottlers, who would normally have a higher operating cost than most small companies, could or would accept 8 percent as a delivery fee.

Question 5. Are you aware of any independent syrup wholesalers that loan equipment for free or at a reduced price?

Answer 5. I am aware of a few (probably less than 10 out of hundreds) independent companies who have loaned equipment in their market. But, this is not their normal business procedure. It has only evolved as a measure to protect their business against competition for a particular account or a chain of accounts. Of these few companies, and my conversations pertaining to these situations, they claim that their margins of profit have eroded and that it is questionable that what they have done has been worthwhile.

Question 6. If S. 2347 is passed, will that result in higher overall costs for fountain beverages to retailers, particularly restaurants and taverns? If so, are those increased costs likely to be passed on to the retailers' customers?

Answer 6. Again, in my over 20 years experience, I have not seen where free or loaned equipment resulted in a reduced price for the consumer. Nor have I seen where a restaurant or tavern was renting or had purchased their own equipment had been unable to sell their fountain products at competitive prices. Soft drinks are probably the highest yielding profitable product a restaurant sells. A single five gallon container of syrup, costing a restaurant less than $30, would return approximately $320. In the last few years we have seen the Southland Corporation, owners of the 7-11 convenient stores, purchase their own beverage systems so they could offer the consumer a wider choice of fountain drinks and they have also made these drinks available to the consumer a very competitive prices, i.e., 79¢ for a 32 oz. cup. I believe another aspect of the competition needs to be addressed in this question. If S. 2347 were passed, wouldn't the major syrup manufacturers be able to reduce

their syrup prices? Currently, they are subsidizing the cost of free and loaned equipment through inflated syrup prices.

Question 7. Do any of your customers who rent fountain equipment from you or own their own equipment offer both Coke and Pepsi, or more than one brand of any flavor of soda? If so, what percentage of your customers do that?

Answer 7. There is a small percentage of our customer base who offer more than one brand of a flavor of soft drinks. Most often these customers are private clubs, like golf, tennis, or social clubs whose members have a say in the products and services that they desire. I would like to compare this to a draft beer. It is not uncommon for restaurants, taverns, or clubs to offer their members and customers a variety of choices, but if the beer companies were allowed to give away equipment (which is against the law), do you think you could get a Miller Lite out of Budweiser equipment?

Question 8. Do both Coke and Pepsi invest in research and development of fountain equipment? If so, in your judgment is that an element of competition between Coke and Pepsi? Could S. 2347 reduce that competition?

Answer 8. Yes! Not only do Coke and Pepsi do equipment research and development, but so do many of us in that beverage dispensing equipment industry. I, myself, have two patents, both directly related to our industry, and my company has been instrumental in the development of special beverage dispensing equipment for the bar and tavern industry. I also know of a number of other independent beverage equipment and service companies who have patents or are involved in the various types of technical research and development to improve existing and futuristic equipment. Every beverage equipment manufacturer has a research and development department. Also, in regard to Coke and Pepsi research and development, I think they, too, are interested in developing new and better methods to either maintain or improve the quality of a dispensed beverage product. One thing which I would question the fairness of, is they will have a manufacturer produce a proprietary product for them to assure that only their "qualified people" can perform service on such equipment.

Question 9. Have you tried to market your fountain equipment to Coke and Pepsi for their use in their free or reduced price equipment programs? If not, why not? If so, what was the result?

Answer 9. For over 15 years that I'm aware of, my colleagues and I have made numerous proposals of ideas and plans, specifically to the Coca-Cola Company and its executive personnel, to absolutely no avail!

We have complained directly to both companies that their free or loan equipment programs were anti-competitive and that we could all serve the consumer market better by their eliminating these programs.

Basically, they have tried to shoo us away like an annoying insect. We have said all along that their *only* concern is market dominance and they don't care how they get it!

Thank you again for your concern in this matter. I hope I have answered your question clearly. Should you have any questions, please do not hesitate to give me a call at area code (617) 639-1005.

Sincerely,

H. RONALD HARRIS,
President.

Senator INOUYE. Thank you very much, Mr. Harris.

In your testimony you indicated that 85 percent of the dispensing equipment was provided by Coke and Pepsi; is that correct?

Mr. HARRIS. No, sir. I say 85 percent of the fountain soft drinks.

Senator INOUYE. That are consumed?

Mr. HARRIS. That are consumed are products of Coke and Pepsi. That leaves, obviously, 15 percent. Of that 15 percent I am not exactly sure where 7 Up's percentage is. RC's percentage is less than four in that part of the market, and I believe 7 Up's is.

Mr. WATKINS. Dr Pepper, 7 Up combined represents an additional ten percent, which means that everybody else represents approximately five.

Mr. HARRIS. And RC is supposedly around three, maybe, at the most. So obviously in the sense that they already, in my opinion and the opinion of many of us here today, they in effect monopolize

the beverage products in the marketplace and they are currently trying to continue to do that by giving away free equipment, which enhances their particular market position in any particular given area.

Senator INOUYE. I did not quite get your testimony at one juncture. You indicate that by a certain year 40 percent of the soft drinks consumed in the United States would be through fountains?

Mr. HARRIS. Would be dispensed through the fountain industry. Today approximately 25 percent of all soft drinks sold are sold through the fountain. As Mr. Griggs alluded to a while ago, he represented an organization that sold 90-some percent of the soft drinks in the country. He was talking, I believe, about total package soft drinks.

The fountain market itself was 25 percent of the total soft drink industry in 1987—1986-1987. In 1986, it was 23-some percent, and it is believed to be at 25 percent today. By the turn of the century, by the late 1900s—1995 to 2000—they believe it will be up to 40 percent.

Again, I believe this is one of the reasons as they—"they" meaning Coke and Pepsi primarily—see the eventual market is developing towards the fountain they have decided to get more active in the market.

Even following up on Mr. Griggs' testimony, I believe he said that the fountain industry was slow in evolving from the bottler's side. If it was not him I believe it was one of the rest of us. I have in my written testimony that I have submitted that the fountain industry was really kind of a stepchild up until about the 1950's. At the innovation, of the fast food restaurant, beginning with McDonald's hamburger stands, is when the primary parent companies started to take a hard look at the development of promoting fountain drinks.

Up until that time it was a very small segment of their industry and now it has grown to 25 percent and they anticipate it to 40 percent, and those are figures that are readily available by just about every source in the industry, related to the soft drink industry.

Senator INOUYE. Thank you very much. As I indicated earlier, we do not anticipate this measure being considered by the Congress this year because we have less than two weeks to go. But we anticipate that this matter will be taken up in the next Congress and in preparation for that, these hearings have been initiated.

If any of you would like to submit additional testimony or make corrections in your testimony, please feel free to do so, but we will close the record 14 days from this day, so you have two weeks.

Mr. HARRIS. Does that mean somebody can speak from the audience now?

Senator INOUYE. No. You can submit written statements.

Mr. HARRIS. Thank you, sir.

Senator INOUYE. With that, I thank all of you for participating this afternoon and the hearing is adjourned.

[Whereupon, at 4 p.m., the subcommittee adjourned.]

OFFICE OF
THE CHAIRMAN

UNITED STATES OF AMERICA
FEDERAL TRADE COMMISSION
WASHINGTON, D.C. 20580

November 17, 1988

The Honorable Ernest F. Hollings
Chairman
Consumer Subcommittee
Committee on Commerce, Science
and Transportation
United States Senate
Washington, D.C. 20510-6125

Dear Mr. Chairman:

The Federal Trade Commission is pleased to submit these comments on S. 2347. The bill, if enacted, would amend section 5 of the Federal Trade Commission Act, 15 U.S.C. § 45, to prohibit certain promotional practices connected with the distribution of post-mixed soft drink dispensing equipment and soft drink syrup. We do not support enactment of S. 2347. The discounting practices that the bill aims to prohibit are probably not anticompetitive. To the extent that some instances of these discounting practices could be anticompetitive, the existing antitrust laws are sufficient to protect competition. Finally, the bill as drafted would be difficult to implement in a way that could promote, rather than restrict, competition.

S. 2347 would make it an unfair act or practice within the meaning of section 5 of the FTC Act for any person engaged in the manufacture, sale, or distribution of post-mixed soft drink dispensing equipment or soft drink syrup to induce soft drink retailers to purchase soft drink syrup from it, to the exclusion, in whole or in part, of other sellers, through certain promotional practices. The prohibited practices include offering retailers equipment, fixtures, signs, or other items without consideration or at less than the fair market value and extending credit to retailers for a period in excess of the customary period in the industry.

But offering free or reduced-price equipment or favorable credit terms are merely forms of discounting from the price at which soft drink syrup is sold to retailers. Some large retailers, such as fast food chains, tend to receive their discounts in the form of lower syrup prices rather than dispensing equipment. Others may receive discounts in the form of deals on equipment. Whether the discount is granted in the form of equipment, cash payments, advertising subsidies, or other items of value on the one hand or a lower syrup price on the

other, the granting of the discount reflects price competition among soft drink distributors.

The fact that the discount takes the form of providing dispensing equipment at no separate charge probably reflects the preferences of the participants in the transactions. For example, according to testimony at the hearings by a major restaurant association, food service operators would have to make larger capital outlays if subsidies for dispensing equipment were prohibited; that larger outlay would be a concern in an industry dominated by small entities with a high failure rate. Some retailers may find it more efficient to purchase their syrup and dispensing equipment from a single source. In addition, the practice may reflect economies of scope enjoyed by soft drink syrup distributors who also provide dispensing equipment.

In the hearings on the proposed legislation, proponents of S. 2347 expressed the view that the granting of discounts through dispensing equipment allowances reflects below-cost, or predatory, pricing. This view, however, assumes that soft drink dispensing equipment and soft drink syrup are two distinct products purchased by retailers and further that the equipment is sold below cost but the syrup is sold at a profit. The transactions might be better viewed as sales of two separate inputs used to produce a final product. Retailers who sell soft drinks seek the minimum total cost per unit of soft drink, and both the syrup and the dispensing equipment are inputs into the final product -- post-mixed soft drinks.

Understandably, some firms may be adversely affected by the form of competition described above. However, syrup sellers that do not supply "free" dispensing equipment can nevertheless compete with firms that do by offering a price on syrup that, when combined with the retailer's expenditures on dispensing equipment obtained from a third party, yields a lower price per unit of post-mixed soft drinks. Equipment marketers could lose customers as a result of syrup sellers' offering discounts in the form of dispensing equipment. That impact, however, may simply reflect the greater efficiency associated with the sale of dispensing equipment and syrup by a single supplier. A similar effect may be observed whenever vertical integration eliminates an intermediate level of distribution. Manufacturers of dispensing equipment, in the aggregate, should not be adversely affected by the practice. These firms would be in a position to sell their products either to soft drink retailers or to syrup suppliers. Indeed, if the practice offers substantial efficiencies, it could increase the demand for dispensing equipment.

We are not aware of a pattern of anticompetitive conduct in this industry in connection with the offering of dispensing

equipment, credit terms, or other consideration to retailers. We recognize that, given certain conditions, it would theoretically be possible for suppliers with monopoly power to use the provision of dispensing equipment as a mechanism for facilitating an efficiency-reducing tie-in among various soft drinks syrups. We have not seen evidence of such practices, however, and the testimony at the hearings on this bill does not suggest that suppliers are providing the equipment to facilitate any such tying arrangement. We note, however, that each of the evils that the bill may address is already a violation of the antitrust laws. For example, predatory pricing violates section 2 of the Sherman Act and the Robinson-Patman Act, tying arrangements that reduce consumer welfare violate section 1 of the Sherman Act and may also violate section 3 of the Clayton Act, and agreements to foreclose competitors from access to essential inputs also violate section 1 of the Sherman Act. In addition, all three types of practices violate section 5 of the FTC Act. Since these practices already are prohibited by section 5 of the FTC Act, there is no need to amend that section to address any anticompetitive practices that may be associated with the conduct addressed by S. 2347.

We also believe that, even if S. 2347 might halt some harmful practices, it is overbroad. It may be that the reduced-price or free provision of dispensing equipment could harm consumer welfare in rare circumstances, but the legislation would essentially erect a per se prohibition of the practice in all circumstances. The proposed legislation does not predicate a violation on a purchaser's agreement not to buy from other suppliers but rather it prohibits the identified equipment discounts or other practices whenever they would have the effect, in whole or in part, of excluding competitors from making a sale to a retailer. For that reason, the bill could proscribe a host of transactions that benefit the seller, the buyer, and consumers. Indeed, the proposed legislation's "in part" language would effectively prohibit offering any discount that is not denominated in dollars per unit of syrup.

This bill illustrates why we think that section 5 of the FTC Act should not be amended to identify specific practices as unfair. The proposed prohibition on offering discounts in the form of signs, supplies, money, services, or credit terms does not appear to address any practice that is intrinsically anticompetitive. Indeed, such non-price forms of competition are common in many industries, including the food service industry. The bill focuses on and indeed would outlaw practices which are normally pro-competitive or benign, without regard to whether the practices actually have anticompetitive effects. Section 5 has served the public interest by allowing the Commission and the courts the flexibility to interpret the antitrust laws in light of current economic understanding of the practices involved.

Encumbering section 5 with definitions of various practices thought to be unfair would deprive the Commission and the courts of that needed flexibility.

Finally, the bill as drafted would be difficult to implement procompetitively. Leasing or selling "at below fair market value" is proscribed but "fair market value" is not defined. If "fair market value" is taken to mean the price charged by others in the market, the effect of the bill would be to eliminate competition. If "fair market value" is taken to mean some cost or profit formula set by statute or government agency decision, the effect of the bill will be to establish a form of government price control. Also proscribed is extending credit to the retailer for a period in excess of the credit period "that is usual and customary." "Usual and customary" is not defined. To the extent that the bill required or promoted identical credit terms it would in fact be dampening a form of competition. It might also be very difficult for a creditor to comply with the requirement, because it is unlikely to have access to its competitors' credit terms.

Please let us know whenever we may be of further service.

By direction of the Commission,

Daniel Oliver

Daniel Oliver
Chairman

Honorable Daniel Inouye
Hart Senate Office Building
U.S. Senate
Washington, D.C. 20510

Attention: Honorable Daniel Inouye

I am writing with respect to the testimony given by Mr. Alfred Griggs, President of the Coca-Cola Bottling Company of Northampton, MA who testified before the Senate Subcommittee in his capacity as Vice Chairman of the National Soft Drink Association. I request that this letter be made a part of the hearing record of S2347.

First let me say again, as I stated in my oral testimony that Mr. Griggs does not represent my views as a member of NSDA or the views of many other members of NSDA who in fact have never been polled with regard to their opinion on this bill. In fact all of Mr. Griggs testimony relates to his knowledge as a Coca-Cola Bottler. No mention is made of Pepsi-Cola's programs.

In addition I would like to make the following observations with respect to his testimony. Mr. Griggs referred to practices of lending dispensing equipment which began in the mid-60's. It should be noted that Coca-Cola USA, a division of the Coca-Cola Company, was in fact the firm that initiated such practices.

The statement that a dollar per gallon in equipment value being placed with a retailer may in fact have been the written word but in actual practice very few accounts received equipment with as little value as $450.00. As a matter of fact it is our personal experience that the average account in the sixties and seventies received well in excess of a $1,000.00 and often upwards of $1,500.00 to $2,000.00. In addition marketing funds were paid to those same retailers who received this equipment on loan, which in essence drove the marketing funds paid per gallon to well in excess of $2.00/gallon. It should also be noted that this program was not available to all customers and was only used where intense competition was involved.

Presently the rule of thumb has been significantly higher than $2.00 per gallon and we have seen it as high as $3.00 and $4.00 per gallon on a regular basis. In addition, Mr. Griggs stated that many independents were paid or reimbursed a fixed amount of money predicated on their gallonage. I must refute this in as much as gallons very often were estimated and the amount of money paid per gallon was often a function of the competition in the

Jason
Jason
CORPORATE HEADQUARTERS
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MEMBER N.B.D.E.A.

marketplace and bore no relationship to sales volume. The funds were paid on projected gallons, but in few instances were the gallons ever adjusted to actual, so in fact the customer was paid well in excess of the actual gallons.

Mr. Griggs also stated that increased cost of equipment gave way to the syrup manufacturers beginning to lease equipment or providing a "bundle program". In fact leased equipment by Coca-Cola USA and Pepsi Cola has not been common over the years and while a lease "agreement" was signed with the lease purportedly paid by the marketing funds generated per gallon of products sold, in rare instances was the customer asked to pay for the shortfall in the lease, if in fact his gallonage was not sufficient to cover that lease. In essence no real cash was ever exchanged. In fact in recent years we have seen not only more equipment being provided, but dollars paid to the customer merely for dispensing the product.

The total value plan ("TVP") which Mr. Griggs made mention of is a new program for Coca-Cola USA. However, it is too soon to tell whether it is in fact being handled uniformly with all accounts. In our marketplace this plan manipulated depending on the competition in the marketplace we have seen. Lease rates are not fixed and while they are recommended, if competition is strong the lease rates have been adjusted significantly.

Lastly, the intense competition within the soft drink industry has done nothing with respect to lowering the price for the ultimate consumer. When equipment and marketing funds are provided to the retailer or food service concern that actually dispenses the product we have found no evidence of benefit to the consumer who buys the product. In fact the retailer most often pockets the difference or just saves on his general overhead.

Its important to note that soft drinks, even with a reasonable rate of return on equipment, (rented or purchased) are the most profitable item on the food service menu. To assume that the consumer who purchases the drink will be adversely affected by low cost or free equipment is in fact erroneous. In the over forty years of business that we have enjoyed in our marketplace we have never found this to be the case.

Respectfully,

Brook R. Jason
President

BRJ:man
cc: Pam Satterwhite

MULTIPLEX®

September 22, 1988

The Honorable Daniel Inouye
United States Senate
Washington, D.C. 20510

Dear Senator:

I am writing to you to express my strong support for Senate Resolution #2347.

The Multiplex Company is the oldest company in the drink dispensing industry and my personal experience spans almost twenty years. I am also a Director of the National Association of Manufacturers and Vice Chairman of their Small Manufacturers' Committee.

Over the past twenty years I have seen the negative results of the practices of the large soft drink franchise companies who have given away dispensing equipment to the detriment of the independently owned and operated manufacturing companies. In the past few years particularly, these oppressive practices have been used to leverage many thousands of small service companies across the country.

The U.S. drink dispensing equipment industry has for years dominated the international market. Almost every manufacturer derives a significant portion of their income from exports. Our company this year was proud to receive the Presidential E for Excellence in Export Award from President Reagan. The continuation of these programs is eroding America's free enterprise manufacturers' core business and threatening the export business.

I want to again express our strong support for your bill and encourage you to continue to push for its passage.

Sincerely,

J. W. Kisling
Chairman and CEO

BCC: H. Ronald Harris

JWK/aeb

MULTIPLEX COMPANY, INC. • 250 Old Ballwin Road • Ballwin, Missouri 63021 • (314) 256-7777 • TELEX: 44-7370

CHUDNOW
MANUFACTURING COMPANY, INC.
SODA FOUNTAIN AND BEVERAGE EQUIPMENT

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November 1, 1988

Senator Albert Gore, Jr. Chairman Consumer Subcommittee
United States Senate
Committee on Commerce, Science, and Transportation
Washington, DC 20510-6125

Re: Senate Bill 2347

Dear Senator Gore,

My name is Mark Chudnow. At the request of Mr. Sandy Hahn, President of Perfection Equipment Corp., I am writing you this letter in an attempt to contribute whatever little input I can to Senate Bill 2347.

I am flattered by Mr. Hahn's description of me as a large fitting manufacturer. We do about $5,000,000 a year with 50 employees. Sales are sinking fast. I am 67 years old and have attained some degree of wealth, the so-called American Dream. My purpose in writing is to try rescuing my company, as well as other small equipment and service companies, from going broke. I have nurtured my company from 1945, my father before me, from a one man operation to its present state. It is as dear to me as my only child.

I am aware of the consequences I might be exposed to writing you in support of Bill 2347. At a coffee klotch, after the hearing of September 28, 1988, the biggest concern by those who supported the Bill at the hearing, was whether they were not burying themselves by testifying. I have watched Senate hearings on television which make me worry about writing you. Two cases of witnesses who were driven out of business by their mentors, after testifying at two separate hearings, still burn in my mind. Nevertheless, I will try to answer the same question as put forth to Mr. Sanford Hahn, as they relate to me.

First I would like to establish that only one of the two cola juggernauts mostly affects the post-mix industry. Post-mix means both soda & flavor dispenses into a cup. Cola giant #2 is really big in the bottled end of the industry which the two giants also monopolize. If you heard or watched the program "60 minutes" last year, the two colas were shown to have paid as high as $300,000.00 for display space in supermarkets. I don't know of any Mom & Pop groceries being offered 10¢ by the Cola's to display their products. Their vying for front door

Continued Page 2.

and shelf space has caused the collapse of many small bottlers as well as syrup manufacturers.

Relating to question #1, we make a complete line of parts for the soda dispensing industry. They can be assembled or used in soda systems or at bars, fast food chains, stadiums, pools, beaches etc. Our "approved" competitors only make either the fittings, regulators, faucets or carbonators. None make more than one of the above. Some counter dispenser manufacturers do make their own faucets and carbonators as well as the refrigerated box they install them in.

In answer to the last three sentences in question #1; yes, we have tried to sell these giants over the years. The results have always been negative. Back in 1964, one of them rejected my regulator, even though it passed everyone of their tests (they sent me the results). The reason was I had an adjustable safety valve when they wanted a non-adjustable one. Meanwhile, they approved one and only one company's regulator which didn't even have a safety. An offer to stake the safety permanently, so as it couldn't be adjusted, fell on deaf ears. Years ago, I tried to submit fittings either directly, through distributors or even through an assumed named corp., to no avail. Again, until recently, they chose one and only one supplier for their fittings even though our specifications were exact and their prices were much higher than ours. In the last 10 years, they have nurtured a new fitting supplier while still retaining their old one. They have set up some steel specifications which their new supplier meets but their old one doesn't; yet they are both approved. I do not feel too rejected since a third supplier has arrived on the scene about 4 years ago, and although meets every present specification, at lower prices, has never been approved. I hear through the grapevine they won't buy from him because he sold his former business, they had set him up in, against their wishes. The reason for being rejected this year was also depressing. I had the very same parts tested by an independent laboratory for the reason they were rejected. The parts tested 100% O.K. including the reasons they were rejected.

Relative to #2. Both colas do not manufacture any equipment of their own. Giant #1 does have a laboratory and also an engineering department. They bestow the benefits of their R & D designs and patents on those chosen few they approve, even though in some cases, the chosen do not even manufacture the part. For instance, I do have one part I make approved by Giant #1. It is a venting valve and is required by law in many states. It was patented in 1976 and was better at 1/2 the price of the existing valve on the market. Giant #1 recently designed one from plastic. You would think they would offer it to their long

Continued Page 3.

time supplier of this product or even two suppliers. Instead, they give it to their favorite son to market even though they do not have the equipment to manufacture it. When they need you they do not worry about approval. In fact, I sell some of their bottlers and even the mother company occasionally without approval.

Relative to #3. The last sentence in question 2 and question 3 are synonymous. Although the colas do buy from independent suppliers, Giant #1, I believe, has some unusual control over most of their major suppliers. I enclose a page from a 1985 annual report from the Lancer Corp. of San Antonio, Texas. You will note practically 100% of Lancers production is Coke. I understand there is another company doing the same thing under 200,000 sq. ft. in Torrington, Conn. Whatever specification or requirements they have are unpublished. As far as I know, they don't exist except at the whim of those in power. They use their test for approval to control or reject those that don't march to their drums.

Question #4 relates to Perfection Equipment only.

Relating to Question #5. I know of no bar, pool, fast food chain, or stadium that reduced their price because they received free or low priced equipment. The only time the consumer benefits from equipment is in the manufacturing field where labor saving devices reflects in the cost of making products and hence a reduction in price. The only time the consumer benefits from these giants is when they buck heads together and compete on a product to product basis.

I believe if Bill #2347 is passed, there will be a more equitable marketplace. The consumer will benefit from the competition of many opposed to a few. New technology will spur new innovations as happened in the telephone industry. At the beginning of this letter I recited my purpose in writing it. If giveaways are to continue, I see the death of the industry from the largest equipment manufacturers to the one man repair shops. I have seen hundreds of syrup manufacturers and service companies, throughout the country, reduced to a mere few because of giveaways. It would break your heart to hear some of these small shop owners crying to me, after years in business, because they have to close shop.

It took me three days and nights to compose this letter and as it was being typed a phone call came in from an old customer who advised me that he could no longer buy tubing from me because he can get it for much less from Giant #1, who sells it to him at cost. To show you how much control this giant has on this industry, you have to know that Giant #1 has service centers throughout the country. (See enclosed letter)

continued Page 4

They use independent servicemen to service and install their giveaway equipment. Naturally, they choose the lowest priced men they can find. They even set these servicemen up in business and let them operate under their service centers roof, therefore eliminating any excess overhead. They provide these servicemen with materials at their cost and dictate how much the servicemen can mark up the parts used in service or installations. Mark ups and service call allowances vary throughout the country. Since most of the equipment in the field is either owned or leased by Giant #1, they become the only game in town. You don't get any of this work unless you dance to their tune. They even have a weird way of billing for parts supplied. Instead of charging the serviceman as he picks them up, they have a system of debits and credits whereby they deduct the cost of the parts from the service or installation work performed.

I thank you in advance for taking the time to read this letter. I have a pet saying to the industry. Because I've been around so long and have sold standard and special parts to every major manufacturer for many years, "More Cola touches something I make, than made by anyone else in the industry". Yet, after 43 years, I am not an approved supplier. Rediculous!!

Thank you again for your indulgance and God Bless.

Respectfully yours,

Mark Chudnow

Chudnow Mfg. Co.
Mark Chudnow, Pres.

October 9, 1988

The Honorable Daniel Inouye
United States Senate
Hart Senate Office Building
Washington, DC 20510

Dear Senator Inouye:

On September 28, 1988, I testified before you in support of S.2347. Time constraints did not permit me to respond to certain statements made by other witnesses who testified in opposition to that bill. Therefore, I would like to take this opportunity to supplement my testimony and have it made a part of the hearing record.

The witness testifying on behalf of the National Licensed Beverage Association stated that "placing soft drink beverage dispensing equipment in a tavern for no charge or at a negligible charge does not create an obligation to purchase the soft drink syrup from the company giving away the equipment." In my 23 years in the soft drink business, I do not know of one instance where the recipient of loaned or free equipment did not feel or act as if they were obligated to exclusively use the products of the company providing the equipment. Indeed, the realities of the marketplace belie the statement that no obligation is created. Supporters and opponents of S.2347 testified that restaurants and taverns using free or loaned equipment do not offer competing fountain cola soft drinks. Over the past few years, however, we have witnessed more and more NLBA members receiving free dispensing equipment from Coca-Cola and Pepsi-Cola. The result is twofold. Equipment and service dealers are losing customers and the consumer has a limited product choice.

It must be emphasized that the proponents of S.2347 are not opposed to bona fide advertising and promotional programs. Our concern stems from the tied arrangement where a retailer accepts free equipment resulting in a contractual or implied obligation to buy only one brand of syrup products. I will discuss later one method used to give away dispensing equipment under the guise of a sales volume program and attach a proposal made by one of the Cola giants.

10624 MIDWAY AVENUE, CERRITOS, CALIFORNIA 90701
213/924-8321 • 714/994-0782

Contrary to the assertion of the NLBA witness, we are not suggesting or seeking an opportunity to market a different brand of cola from a Coke or Pepsi dispenser. Rather, we are seeking the elimination of inducements, which in turn eliminate the consumer's ability to choose among soft drinks by excluding competitive syrups. We are also trying to preserve the economic viability of hundreds of companies and thousands of jobs.

One witness testifying against S.2347 stated that the free equipment was a part of a general marketing program earned by the retailer -- implying there was no free lunch. We agree there is no such thing as "free" equipment. The cost of the "free" equipment given away by Coca-Cola and Pepsi-Cola, in my opinion, is subsidized by higher syrup prices to retailers and ultimately is paid for by the consumer. By eliminating the "free" equipment, Coke and Pepsi could lower the price of their syrups.

Another argument raised at the hearing was to the effect that denying free equipment would hurt the profits of retailers. The economics of the fountain drink business refute that argument. Fountain dispensed soft drinks are one of the most profitable products sold by restaurants, outside of iced tea. According to the testimony of Mr. Crawford of the National Restaurant Association, "7 out of 10 eating and drinking establishments have gross sales of less than $500,000 annually." These restaurants, he said, would be "hard hit" by increased costs of equipment. Nothing could be further from the truth. These restaurants would normally be able to lease equipment for approximately $600 per year including service and maintenance. Profit from 5 gallons of syrup is approximately $275 and even the smallest establishment uses over 300 gallons of syrup a year, giving them a minimum profit of $16,500 just on their fountain drink sales. To suggest that banning free equipment would cause retailers to be "hard hit" is not borne out under close analysis.

Similarly, the argument that S.2347 would hurt research and development of dispensing equipment and impede the placement of updated equipment in restaurants, bars, and taverns is not valid. This argument fails to recognize that the bulk of research and development in soft drink equipment has been undertaken by the companies that manufacture and service the equipment -- the industry we are trying to preserve -- not by Coca-Cola and Pepsi-Cola who like to have an exclusive manufacturing arrangement with one or two manufacturers.

Improving the quality of the equipment used to dispense soft drinks permits us to market and service the new and improved equipment. It is ridiculous to suggest that our industry offers outmoded equipment for lease or sale whereas Coca-Cola and Pepsi-Cola give away state-of-the-art equipment. I can compete with the quality of any equipment offered by Coca-Cola or Pepsi-Cola, but I cannot compete with their free placement programs. For my company to lease or sell old equipment would be like Hertz trying to rent old cars.

As I mentioned earlier, I am enclosing a copy of a proposal made by Pepsi-Cola to a Mexican food restaurant chain in the greater Los Angeles area called Red Onion. This proposal is similar to many others we have seen over the past few years from both of the two giants.

Although these proposals generally have the appearance of being designed to attract a potential customer's business, they are usually an exercise in who will promise to give the most to get the customer to buy their products. This proposal, like most, is based on Coca-Cola and Pepsi-Cola creating exaggerated potential volumes of usage by the restaurant chain that then enable the proposer to inflate the advertising and marketing allowances that they can initially promise the account.

This, of course, is very deceptive competition, because the potential customer is only looking at the bottom line and will intentionally overlook the exaggerated volumes in order to receive the "advance" marketing funds. Once the customer has accepted a proposal such as this, they become locked into a long-term arrangement. Because of the exaggerated volumes, however, the customers seldom, if ever, receive all of the money shown in the proposal.

Although this particular proposal to Red Onion does not directly and specifically offer free equipment, it does show the methodology of a deceptive approach the parent companies take to lure an account into the fold.

For example, in 1986, Red Onion had 14 locations. This proposal, which begins in 1987, is based on 18 locations. Part of the deception here is that in 1986 there wasn't any conceivable way for the chain to open four new restaurants in 1987, much less four more locations in each succeeding year of the proposal.

Secondly, the volume of 27,000 gallons for the two products that Pepsi-Cola proposes they sell is ridiculously overstated based on the fact that in 1986 Red Onion purchased approximately 15,000 gallons from my company, as we were their supplier. This amount can be substantiated from our sales records.

The proposal offers $27,000 just for the conversion to two Pepsi-Cola products plus an additional $13,500, called marketing funds, for a total of $40,500. These sums would be paid upon Red Onion's signing a 5-year exclusive agreement, the conditions of which the restaurant chain could never meet.

In conclusion, let me say that S.2347 is neither unique nor anti-competitive. In fact, it will enhance competition in a market that is rapidly becoming the exclusive domain of two companies. The practices S.2347 will eliminate, Congress found objectionable with respect to alcoholic beverages in 1935 when it enacted the Federal Alcohol Administration Act, 27 USC Section 205. Further, Wisconsin has enacted legislation which prohibits the giving away or loaning of soft drink equipment, and California law makes it an unfair trade practice for the dairy industry to give away equipment (Cal. Food and Agricultural Code, Art. 4, Section 61375(a)).

Sincerely,

H. Ronald Harris
President

HRH: mrw

Enclosure 1/

1/ The enclosure was not reproducible.

TELEPHONE (203) 589-4050

THE DAVID SODA dispensing co.

Carbonating Equipment
Service and Supply

P.O. BOX 9338 — FORESTVILLE, CONNECTICUT 06010

OCTOBER 10, 1988

HONORABLE SENATOR D. K. INOUYE
UNITED STATES SENATE
ROOM 722
HART SENATE BUILDING
WASHINGTON, DC 20510

Dear Senator Inouye:

I enjoyed observing the U.S. Senate process while attending your hearing last week on S 2347.

To further illustrate what is happening to the small businessman, I am enclosing a copy of an "AGREEMENT" between The Elks Club Of Bristol, CT, a former customer of mine, and Pepsi Cola DBA Elco Beverage Company of Bristol, CT.

The David Soda Dispensing Co. had leased beverage dispensing equipment to The Elks Club since 1979 until last year when The Elks received an offer they could not refuse.

Our lease price to the Elks was $936.00 per year.

On August 26, 1986 The Elks requested termination of their lease with our company.

On September 22, 1986 The Elks House Committee met with us for the purpose of reviewing their contract with us.

On December 23, 1986 The Elks told us they would not renew their contract with us.

The Elks advised us that Pepsi Cola (Elco Beverage) made a proposal that they could not refuse. Enclosed is a copy of that agreement whereby the lease price of $1040.00 per year appears to be slightly higher than our lease price of $936.00 per year. However, Pepsi Cola waived $520.00 of the lease price as a donation. The net billing to The Elks for record purposes is $520.00 per year, a price below cost.

We, as a small business, find it impossible to compete with below cost pricing and urge your committee and the Congress to enact S 2347.

Sincerely,

Jesse J. Gersten
JJG/bh
Enclosure

Member of: NATIONAL BEVERAGE DISPENSING EQUIPMENT ASSOCIATION

nsda
NATIONAL SOFT DRINK ASSOCIATION

SWANEL BEVERAGE DISPENSERS
P. O. BOX 1186
HAMMOND, INDIANA 46325
(219) 932-7676 (312) 786-2066

October 5, 1988

Senator Daniel Inouye
Senate Office Building
Washington, D.C. 20510

Re: Bill S-2347

Dear Senator Inouye:

Last week we attended the Senate hearing on Bill S-2347, regarding the policy of giving away free beverage dispensing equipment by major soft drink companies. As members of CEEGA, the Committee to End Equipment Giveaways, we fully support the passage of this bill. Swanel, Inc. is a small family-operated business, with 30 employees, operating in the Chicago metropolitan area for 46 years. We are directly and adversely affected when companies such as Coca-Cola and Pepsi-Cola offer free equipment to lure away our customers.

Attached is a copy of a proposal from Pepsi-Cola to Schoop's Hamburgers. It illustrates the type of problem we face and defines their program and the large amount of money our customer would realize if they switched to Pepsi products. A small, developing franchise organization such as Schoop's would find it difficult to resist a free gift of $116,000, even if the figure may be misleading or unrealistic. Again, this is just one example of the type of problem we often encounter.

We foresee a future for the soft drink industry in which 2 or 3 companies will totally dominate in the Chicagoland area if Bill S-2347 fails to be enacted. Small and medium size companies will be forced out of business or to significantly alter the focus of their business. We urge you to support the passage of this bill.

Sincerely,

Albert Roviaro
President
Swanel, Inc.

Sodibar Systems

October 10, 1988

The Honorable Daniel Inouye
Hart Senate Office Building
U S Senate
Washington, D. C. 20510

Dear Senator Inouye:

As a supporter of Bill S-2347, it was a pleasure to see so many other indpendent businesses in attendance of the hearing and in favor of this bill at the Senate hearing. Unfortunately, there is not enough time in a day or days in a week to hear all the feelings of the post-mix beverage distributors who are being financially strained or put out of business because of equipment give-aways.

My primary reason for writing to you is to express my concern of the statements of two different witnesses who testified at the Senate hearing. The first being that of Mr. Sandy Hahn from Perfection Equipment Company of Gurnee, Illinois. Mr. Hahn was absolutely correct stating that his company lost the bid for the new food service facility at the National Air & Space Museum. After Coca Cola, USA, decideed it was in their best interest to secure that business, they "loaned" them soda dispensing equipment to guarantee Coca Cola products would be dispensed. In turn, my company was issued a purchase order to install the equipment and send Coca Cola, USA, the installation invoice of approximately $20,000.00. Again, another example of syrup business being secured through an equipment give-away program instead of fair marketing practices.

The other concern of mine is the testimony of Mr. Eugene J. Meigher, the anti-trust attorney from the law firm Arent, Fox, Kitner representing the National Soft Drink Association. I can understand his concern for eliminating free equipment from syrup manufacturers. If free equipment had not been available, his firm probably would have had to rent or purchase their soda dispensing equipment that Coca Cola, USA, "loaned" them and paid us to install and service. I think a firm the size of Arent, Fox, Kitner would have the funds to purchase or rent their beverage dispensing equipment and not be forced to use specific brands becaused they have "loaned" dispensers.

It is difficult for me to understand the competitive necesity of placing free equipment in a law firm. There is surely not high visibility in an account such as this.

After more than 20 years in this business that my father started 40 years ago, I surely hope my children will carry it on for its 80th anniversary some day. However, if S-2347 is not passed, then there is little chance of existing in the future. I request that my comments be included in the hearing records of S-2347.

Sincerely,

Sodibar Systems

MAS:eje

Mark A. Simon
Vice-President

FEDERAL SUPPLY CO.

FOODSERVICE EQUIPMENT AND SUPPLIES

October 14, 1988

Mr. Sandford Hahn, President
Perfection Equipment, Inc.
4259 Lee Avenue
Gurnee, IL 60031

RE: Invoice # 19190 of 9-15-88

Dear Sir:

We have been recently contacted by our client who expressed an interest to cancel all equipment purchased against above referenced invoice and requested that we contact you for permission to do so. As it turns out the cancellation of this order is not because they are no longer intending to use this product but because their soda supplier (ie: Pepsi Cola or Coca Cola) are willing to furnish them comprable equipment on a no charge basis as long product is purchased from them. They further informed us that their supplier will continue to leave this equipment on their premises on a no charge basis and service same for a nominal amount of $ 25.00 per month as long as the buying agreement is in force.

Unfortunatly, this is not an isolated incident and we are seeing more and more occurances of this nature depriving dealers such as ourselves, of sales and corresponding profit. This to me represents an unfair competitive advantage and your views on this and similar situations would be appreciated.

Sincerely yours,

D. N. Selevredes

Demetrios N. Selevredes, Sales Manager
FEDERAL SUPPLY COMPANY

dns/db

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OCT. 17 1988